DOCUMENT RESUME

ED 059 453 AC 012 325

AUTHOR	Litecky, Paul A.
TITLE	Franchising. Instructor's Manual.
INSTITUTION	Small Business Administration, Washington, D.C.
REPORT NO	Topic-18
PUB DATE	[68]
NOTE	82p.; Management Development Program
AVAILABLE FROM	Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402 ($1.75); Small Business Administration, Washington, D. C. 20416 (on loan basis)
EDRS PRICE	MF-$0.65 HC-$3.29
DESCRIPTORS	Administrative Personnel; Audiovisual Aids; Bibliographies; Business Administration; Case Studies (Education); *Cost Effectiveness; Course Content; Distributive Education; *Educational Programs; Industry; Instructional Materials; Lecture; Lesson Plans; *Management Education; *Manuals; Participant Characteristics; Professional Continuing Education; Stimuli; *Teaching Guides; University Extension
IDENTIFIERS	*Franchising

ABSTRACT

The third booklet in a second series of subject presentations intended to advance the effectiveness of small business management is presented. The lecture is designed as the basis for a presentation to the businessman in nontechnical language. The Lesson Plan is an outline of the material covered which may be used as a teaching guide or as a framework for developing an individualized presentation. The Presentation is a carefully prepared subject presentation which may be used as written or modified to meet local needs and conditions. Visual Aids are photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The Supply Department consists of materials which can be reproduced locally for distribution to course participants. Cases in Point are short actual small-business management cases which may be used to augment the presentation and to develop discussion. The Incubator is a source of ideas for further thought and discussion by the participants. A short bibliography is provided, and field offices of the Small Business Administration are listed. (CK)

ED 059453

U.S. DEPARTMENT OF HEALTH,
EDUCATION & WELFARE
OFFICE OF EDUCATION
THIS DOCUMENT HAS BEEN REPRODUCED EXACTLY AS RECEIVED FROM THE PERSON OR ORGANIZATION ORIGINATING IT. POINTS OF VIEW OR OPINIONS STATED DO NOT NECESSARILY REPRESENT OFFICIAL OFFICE OF EDUCATION POSITION OR POLICY.

SCOPE OF INTEREST NOTICE
The ERIC Facility has assigned this document for processing to: AC
In our judgement, this document is also of interest to the clearinghouses noted to the right. Indexing should reflect their special points of view. VT

F-7

FRANCHISING

INSTRUCTOR'S MANUAL
MANAGEMENT DEVELOPMENT PROGRAM
SMALL BUSINESS ADMINISTRATION

TOPIC EIGHTEEN

A 1902 FRANCHISE.

AC012325

SUBJECT PRESENTATIONS
in the
SMALL BUSINESS MANAGEMENT DEVELOPMENT PROGRAM

Small Business Administration

Subject presentations and a set of overhead projection transparencies for each are available on loan from SBA regional offices to cosponsors of management training courses, conferences, problem clinics, and workshops. The topic number and title of the presentations now available in each series are listed below.

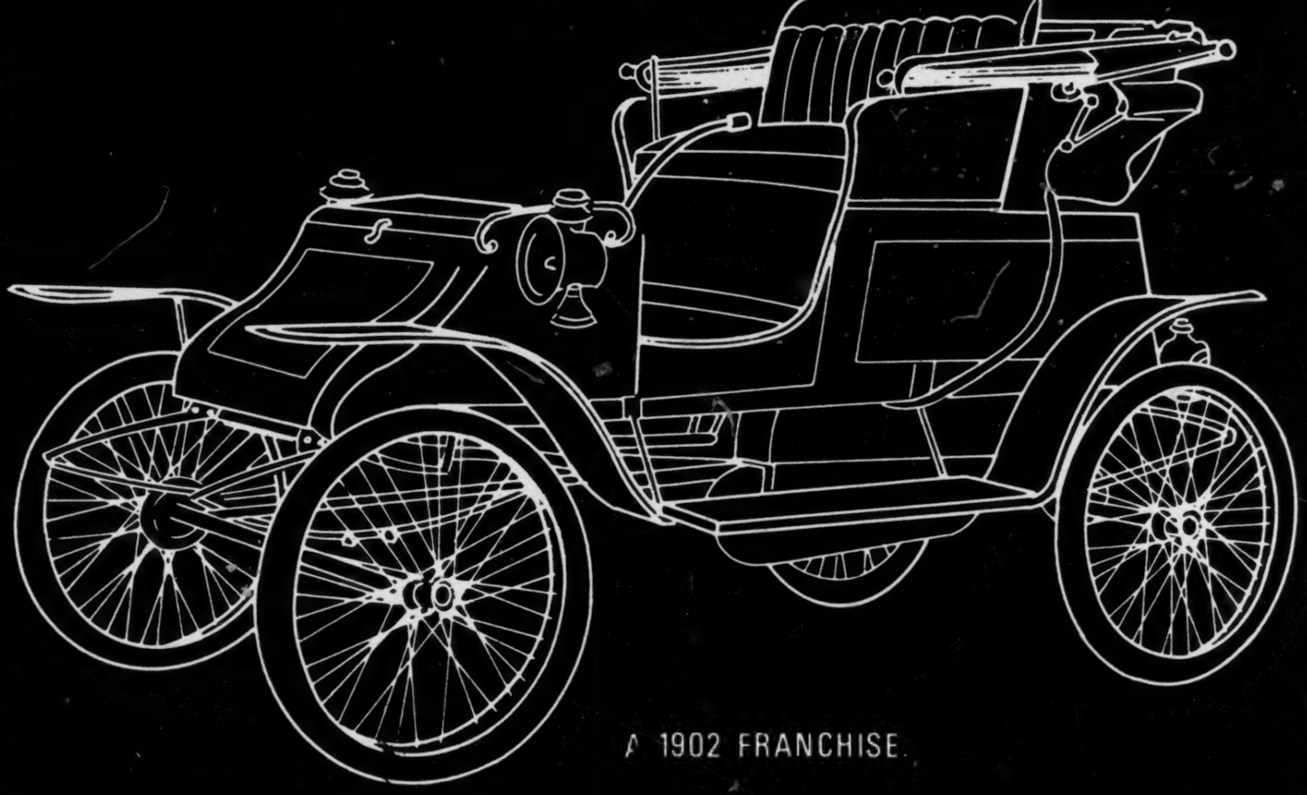
Topic No.	*Title*
	First Series
1	Success and Failure Factors
2	Records and Credit in Profitable Management
3	Managing to Sell
4	The Why and What of Bookkeeping
5	Financing Long and Short-Term Needs
6	Personnel Management
7	Special Aspects of Sales Promotion
8	Taxation: A Key Factor in Business Decisions
9	Communication and Control
10	Human Factors in Small Business
11	Choosing a Form of Business Organization
12	Safeguarding Your Business and Management Succession
13	Small Business Location and Layout
14	Effective Advertising
15	Sources of Assistance and Information
	Second Series
16	Why Customers Buy (and Why They Don't)
17	Marketing Research
18	Franchising

NOTE: These may be purchased from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402; or from the U.S. Department of Commerce field offices. Price: $1.25 each for Nos. 1, 2, 6, 7, 8, 14, 16; $1.50 for Nos. 3, 4, 5, 9, 10, 11, 12, 13, 15, 17; $1.75 for No. 18. Catalog No. SBA 1.24.

FRANCHISING

INSTRUCTOR'S MANUAL
MANAGEMENT DEVELOPMENT PROGRAM
SMALL BUSINESS ADMINISTRATION

TOPIC EIGHTEEN



A 1902 FRANCHISE.

SMALL BUSINESS ADMINISTRATION

Howard J. Samuels, *Administrator*

PROCUREMENT AND MANAGEMENT ASSISTANCE

Irving Maness, *Associate Administrator*

OFFICE OF MANAGEMENT ASSISTANCE

Clyde B. Bothmer, *Acting Director*

EDUCATION DIVISION

Wendell O. Metcalf, *Chief*

For sale by the Superintendent of Documents, U.S. Government Printing
Office, Washington, D.C. 20402 - Price $1.75

FOREWORD

This presentation on a critical subject of growing importance to small business enterprise is another forward step in the continuing efforts to strengthen our Small Business Management Development Program. The program was developed by the Small Business Administration to bring sound management knowledge and techniques to the owners and managers of small businesses. Rapid progress of this management education undertaking has been realized through cooperation of educational institutions and business associations throughout the Nation. In 15 years, more than 8,700 courses, conferences, problem clinics, and workshops have been cosponsored with over 2,000 universities, colleges, local school systems, trade associations, chambers of commerce, and other business organizations. Approximately 370,000 owners and managers, and prospective owners and managers, of small businesses have received training in this program.

This is the third booklet in a second series of subject presentations intended to advance the effectiveness of small business management.

Each of these booklets presents, for educators and businessmen who teach management to small business owners and managers, a complete one-session subject presentation, including a lesson plan, lecture, visual aids, case studies, selected bibliography, and handout material. This material should be of assistance in establishing new management programs and in maintaining existing ones, particularly by emphasizing the importance of continuing education for small business owners and managers and by assisting the busy instructor with his preparation.

This presentation on *franchising* may find application with cosponsors in other SBA programs such as those dealing with training prospective business owners among the disadvantaged, disaster loan assistance in reestablishing small businesses, management assistance counseling, equal opportunity, and the dislocation of small businesses resulting from urban renewal and highway construction. This presentation has particular significance for programs that promote minority ownership of inner city business.

The preceding SBA series of administrative management subject presentations resulted from a recommendation of a committee on management education, representing the Small Business Administration and the Distributive Education Division of the American Vocational Association. It consists of 15 booklets identified by "Topic 1" through "Topic 15."

Enthusiastic utilization of the first subject presentations demonstrated the need for this type of package treatment and a second series was planned. The present management development series continues the number sequence and begins with *Topic Sixteen,* "Why Customers Buy," followed by *Topic Seventeen,* "Marketing Research." This one titled "Franchising," therefore, is *Topic Eighteen.*

The author, Paul A. Litecky, is a recognized specialist in business communications and is presently employed as a consultant to business and government in audiovisual communication techniques. Artwork and visuals were designed and produced by James W. Truett, Jr.

This publication was prepared with the supervision of Dr. Weston R. Clark, education specialist, and the administrative direction of Wendell O. Metcalf, chief, Education Division.

HOWARD J. SAMUELS,
Administrator.

CONTENTS

Page

Foreword iii

A Word About This Session vii

The Lesson Plan 3

The Presentation 5

Visual Aids*. 23

The Supply Department**. 27

Cases in Point 63

The Incubator 67

Bibliography 67

---

*A set of the visual aids is available from the nearest SBA regional office (see inside back cover for listing). These visuals are 8- by 10-inch colored transparencies for use on overhead projectors.

**Among the materials prepared as "handouts" to participants are several SBA free publications. Current information on the availability of suggested and new SBA publications may be obtained from the nearest SBA office.

A Word About This Session

"Franchising," *Topic Eighteen,* was prepared to aid in teaching one session of a small business management course, conference, clinic, or workshop. It contains sufficient material for a 45- to 60-minute lecture which is usually followed by a discussion period. The management cases, incubator items, and significant information which might be drawn from the handout material and the bibliographical sources can be used to extend the session or as a basis for successive sessions on the topic.

The lecture is designed as the basis for a presentation to the businessman in nontechnical language. It represents *one* teaching approach to franchising. It is expected that instructors may wish to modify or revise the lecture material according to their personal background and experience in the subject area. They may also find it desirable to supplement or adjust the treatment in order to meet more effectively the training or special needs of their participants.

Should time limitations necessitate shortening the presentation, selected changes are feasible. Suggestions include deleting parts of Types of Loans in part IX, and condensing the treatment of legal counsel services in part VIII and the source of franchise opportunities in part VI. Such modifications could be made without destroying an effective sequence of subject treatment.

This topic can best be handled by one who has special knowledge in the subject of franchising, is familiar with small business, and is experienced in conducting training sessions for small business owner-managers.

Persons or organizations interested in cosponsoring small business management training, such as courses, conferences, workshops, or problem clinics, may be provided on loan a selection of needed subject presentations, and a set of overhead projection transparencies for each, from the nearest Small Business Administration field office. SBA offices are listed on the inside back cover. Titles of available booklets in the first and second series appear on the back of the front cover. Single booklets or complete sets may be purchased from the Superintendent of Documents, Government Printing Office, Washington, D.C. 20402.

The various sections of this booklet are separated by divider sheets of different colors. These colors are given here, and the contents of the sections are briefly described.

Gray—*The Lesson Plan.* An outline of the material covered which may be used as a teaching guide, or as a framework for developing an individualized presentation. The lesson plan contains two columns: The left-hand column is an outline of the presentation; the right is a step-by-step indication of procedure, including chalkboard suggestions, quotations, discussion points, and a keyed guide to the visual aids supplied.

Rust—*The Presentation.* A carefully prepared subject presentation which may be used as written or modified to meet local needs and conditions. It may also be used as a source of information by a person preparing his own lecture.

Buff—*The Visual Aids.* Photographic copies of the set of visual aids which are available for this topic. These visuals are 8- by 10-inch colored transparencies prepared for use on overhead projectors. The subject presentation and lesson plan are keyed to the visuals. A set of visuals for each subject in this series may be borrowed from the nearest SBA regional office.

Green—*The Supply Department.* Materials which may be reproduced locally for distribution to course participants. Your nearest SBA office can furnish information on current availability of SBA free publications, including titles published subsequent to this volume.

Yellow—*Cases in Point.* Short actual small-business management cases which may be used to augment the presentation and to develop discussion, or as the basis for a second session on the same topic.

Blue—*The Incubator.* Ideas for stimulating further thought and discussion by the participants. This material may be reproduced locally for distribution to course participants. "Assignments" are designed to aid in retention of the subject matter of the session.

NOTE: See back cover for index reference to the divider sheets.

INSTRUCTIONAL FORMAT SHOULD BE STIMULATING

Use The Three B's

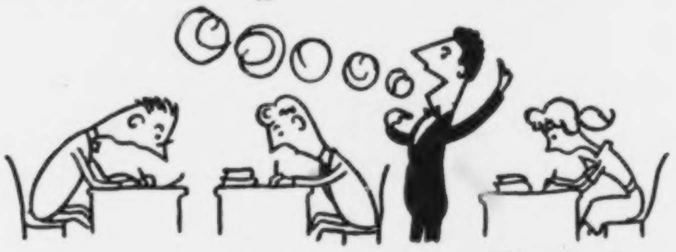
- ***Base*** instruction on problems at learners level.
- ***Blend*** instruction with job experience.
- ***Brighten*** instructions with variety of ***illustrations, investigations*** and group ***participation.***

FOUR BASIC STEPS OF INSTRUCTION

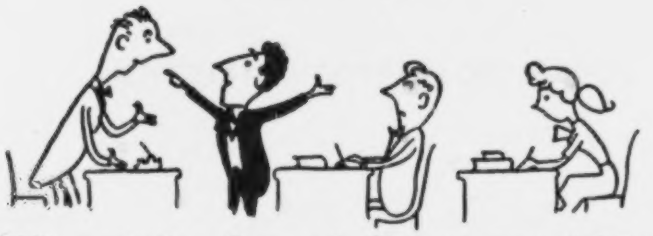
Instructing is like selling - -

Selling	**Instructing**
1. Approach customer	1. Prepare the group
Promptness	Start on schedule
Put at ease	Put group at ease
Awaken ***interest***	***Awaken*** interest
2. Present merchandise or service	2. Present information
Select merchandise to fit need	Gauge material to needs
Show one item at a time	Present one point at a time
Demonstrate ***selling points***	***Show, illustrate, question***
3. Have customer take part	3. Have group participate
Get merchandise into customer's hands	Get group to ***discuss***
Let customer "try on" merchandise	Have members ***demonstrate*** or ***use*** ideas
Answer questions and meet objections	Answer questions and correct errors
4. Bring sale to close	4. Bring meeting to a close
Help customers decide; ask:	Check on understanding; ask:
"which"	"why" "how"
"for whom"	"when" "what"
"when"	"where" "who"
Be sure merchandise fits need	Be sure group now can use information
Summarize points of care and use	Summarize "take away" ideas
Handle mechanics of sale	Make a definite conclusion
Pave way for return visit	Pave way for next session

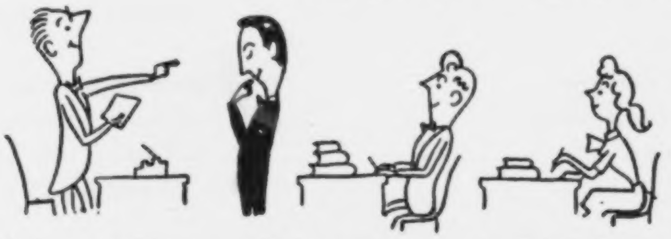
How To Deal With "Difficult Customers"



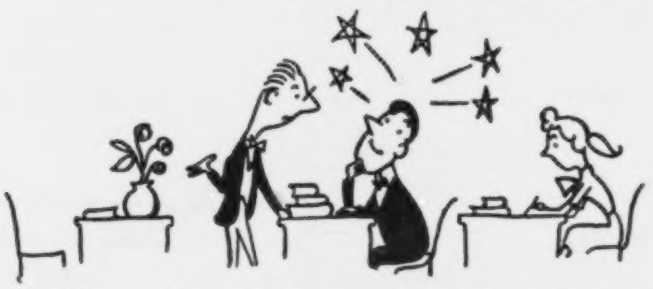
	What To Do
THE "MOUTH"—wants to do all the talking.	**Take the play away from him by asking others to comment on his remarks.** **Deliberately turn to others and ask for their opinions. Avoid looking at him.** **Tactfully ask him to give someone else a chance, or talk to him in private.**



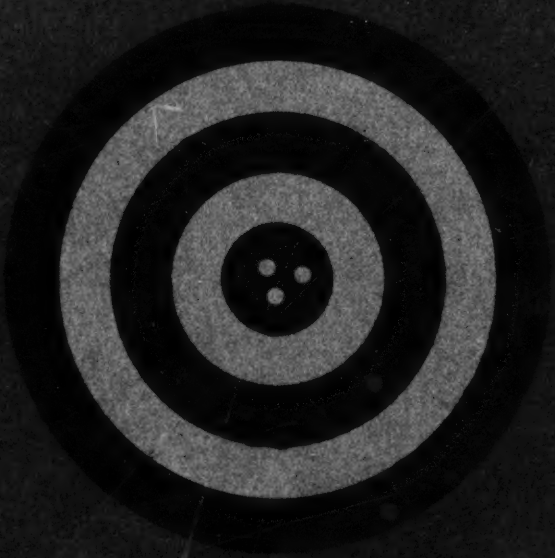
THE "ARGUER"—constantly tries to catch you up.	**Keep cool. You can never "win" an argument. Always make him back it up. Ask for evidence.** **Avoid getting personal.** **Refer the question to the group and then to him.**



THE "MOUSE"—is in every group.	**Call him by name and ask him for an opinion. Ask him an easy question he is sure to answer well, then praise him. This person is worthy of your attention.**



THE "SO-WHATER"—is disinterested.	**Point up something he has done as a good example of the point being stressed. Ask direct questions affecting his work.**



THE LESSON PLAN

A Keeping on Target

Section

Good teaching depends on good planning. A session objective or target must be set. Then the points are selected that will enable one to keep hitting at the heart of that target.

The primary aim of the instructor is to first give the participant the things he MUST KNOW, then the things he SHOULD KNOW. When these two aims have been achieved, the topic can be embellished with the like to know and helpful to know elements.

The following lesson plan is "on target." If it is used as a guide, it will enable the instructor to emphasize the major points while at the same time he stimulates the participants to grasp the subject.

LESSON PLAN

Topic: Franchising

Objectives: To examine the system of distribution that binds a group of small businesses into the image and marketing style of a chain.

To determine the benefits derived from the use of a franchise system of distribution for both the franchisor and franchisee.

To set up guidelines for evaluating franchise opportunities.

Session Content	Tips and Approaches
I. Introduction	Use Visual No. 1.
II. The Anatomy of Franchising	Visual No. 2.
A. Definition of franchising	Visual No. 3.
1. Franchising of products	
2. Franchising of entire business enterprises	
B. How franchising works	Visual No. 4.
	Visual No. 5.
C. Why franchising works	Visual No. 6.
III. Advantages of Franchising	
A. To franchisor	Visual No. 7.
B. To franchisee	Visual No. 8.
IV. Disadvantages of Franchising	Visual No. 9.
A. To franchisor	
B. To franchisee	
V. Where to Find Franchise Opportunities	Visual No. 10.
A. Annual directories	
B. Daily newspapers	
C. Trade publications	
D. Franchising publications	
E. Franchisor exhibitions	
F. Franchise marketing agencies	
VI. Evaluating a Franchise Opportunity	Visual No. 11.
A. Investigate before investing	
1. Investigate the company	
2. Investigate the product	
3. Investigate the territory	
4. Investigate the contract	
5. Investigate continuing assistance	
B. Control as a mutual exchange of values	Pass out handout, evaluating a franchise.

VII. Legal Counselling

- A. Need for legal counsel
- B. Services of legal counsel
  - 1. Checking
  - 2. Advising
  - 3. Guiding
  - 4. Representing

Visual No. 12.

VIII. Financial Assistance

- A. Capital requirements
- B. Lending institutions
  - 1. Banks: Types of loans
    - a. Straight commercial loans
    - b. Character loans
    - c. Term loans
    - d. Collateral loans
  - 2. Veterans Administration
  - 3. Small Business Administration

Visual No. 13.

IX. Management and Technical Aid

- A. Promotional support
- B. Recordkeeping systems
- C. Training programs for franchisees

X. Summary

THE PRESENTATION

A What to Talk About

Section

The presentation outlined in this section may be used in at least one of three ways:

1. As a reasonably complete lecture which may be modified to meet local needs and conditions.
2. As reference material.
3. Merely as a guide for the coordinator or the speaker. (The experienced discussion leader may wish to [illegible] plan and develop a presentation based on his own wealth of knowledge and experience.)

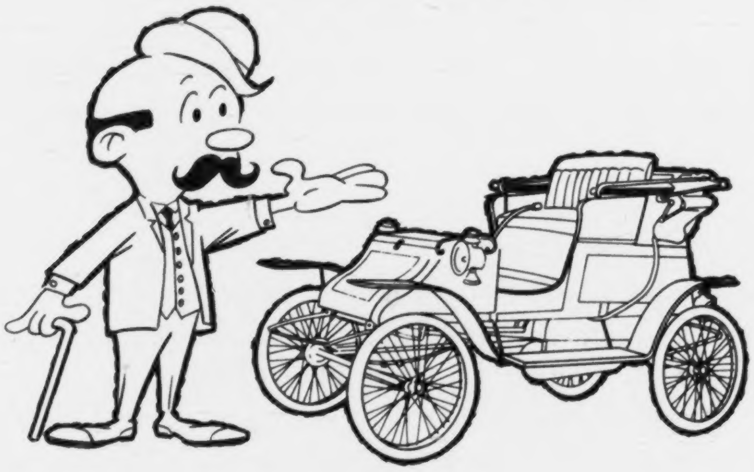
It is hoped that the principal points in the presentation will be covered. This will insure a degree of uniformity in the program as a whole, while leaving the coordinator and speaker a large measure of flexibility.

FRANCHISING

Have you ever been driving at some distance from your own stamping ground and noticed one familiar sign after another? A restaurant, a drive-in, an auto supply store, an ice cream stand, and others—all with the same name and much the same appearance as similar stores in your home community? Most of these businesses, although they vary widely in what they offer, have one important common denominator. Each one is a franchise business.

Franchising is not new to the marketplace. In fact, one of the first examples of what we consider franchising was the licensing of an independent dealer to sell and service electric and steam automobiles in 1898. In the 1940's, the principal franchising operations were the ones run by auto manufacturers, soft-drink companies, and the oil refineries. The most phenomenal growth of franchising has taken place since World War II.

EARLY FRANCHISE BUSINESS

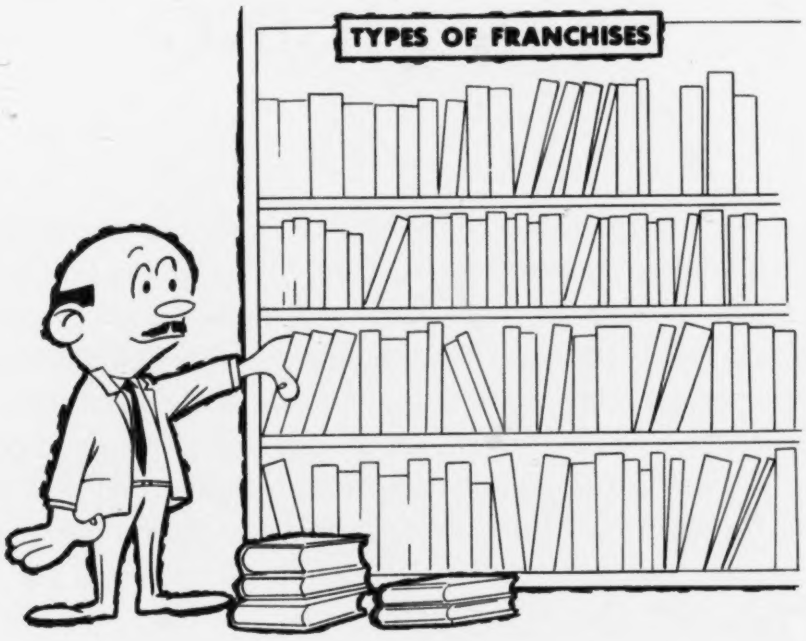


Visual 1

Today just about everything is, and can be franchised, including drycleaning, motels, ice cream, rental cars, laundromats, even secretaries. Indeed, the variety of business activities ranges from advertising specialties to water softeners, with an almost unbelievable selection of business types to choose from.

In 1967, more than 750 companies reported a total of 450,000 franchised businesses in operation. And the number of franchise-holders is growing at the phenomenal rate of 40,000 a year. Certainly a part of the reason for this exciting growth is the impact of success stories that are common to franchising. People *have* "struck it rich" with franchised businesses.

A New England taxi driver parlayed a $10,000 investment in a snackbar franchise into a $250,000 equity. An $87-a-week insurance clerk from New York answered an ad for a food specialty franchise in Brooklyn. His first year's net profit was $15,000. His second year $20,000. And he's just beginning to hit his stride. Similar stories crop up wherever franchise business is being discussed. Of course, there are also many stories of disappointment, financial loss, or *even* complete failure. But franchising *can* be the means for a moderate-income individual to develop financial independence with a minimum investment.



Visual 2

THE ANATOMY OF FRANCHISING

Franchises are available today in such a variety of sizes and shapes that it is necessary to "go back to the beginning" to develop a clear understanding of what we are looking at.

Definition of Franchising

First of all, let's describe franchising.

In actual practice, the franchise is usually a contract to distribute and sell goods or services within a specific area. The franchise business is owned by an individual and operated by him as a part of either a national, regional, or local chain of businesses.

The franchise agreement often gives the franchise holder the exclusive right to sell for, or otherwise represent, the parent firm in the selected area. In return, the franchisee contracts to

DEFINITION OF FRANCHISING

FRANCHISING IS THE SYSTEM OF DISTRIBUTION WHICH ENABLES A SUPPLIER (FRANCHISOR) TO ARRANGE FOR A DEALER (FRANCHISEE) TO HANDLE HIS PRODUCT OR SERVICE UNDER CERTAIN MUTUALLY AGREED UPON CONDITIONS.

Visual 3

pay either a specific sum of money (the franchise fee), or a commission on gross sales, or he guarantees to buy equipment and supplies from the franchisor, or some combination of these considerations.

Franchising of Products

A simple franchise arrangement exists when a manufacturer practices selective or exclusive distribution of his product—in *other* words, utilizes a *product franchise.* A typical example of this system of distribution is an automobile agency.

The retail dealer desires to have the supplier's franchise—the exclusive right to sell the supplier's product line. The retail dealer is normally quite willing to concentrate his selling efforts toward the franchised products because they offer him good, stable profit opportunities. All customers desiring to trade in his franchise area must come to him for the product.

Normally, the retailers holding product franchises operate under their own business name. They are *not* identified as members of a group, and they follow their own methods of operation, which quite naturally vary greatly from one retailer to another. In fact, quite often the franchised product line may only be used to round out the retailer's other offerings, and is not the only product he sells—witness the number of RCA or General Electric dealers in your city. The control exerted over the retailer by the supplier in such franchises is small and is limited to the one particular franchised product and *not* to the operation of the business itself.

Franchising of Entire Business Enterprises

In the more commonly understood sense, franchising is taken to mean the licensing of an individual to conduct a specific type of business according to a predetermined pattern developed and perfected by the franchisor.

The franchised establishments which operate within a particular franchise system are usually identified as members of a group. They operate under a common trade name—for example, Chicken Delight, Dunkin' Donuts, MacDonald's and so on. Their business operation, their establishment's appearance, their merchandise—even their operating procedures are standardized to a very high degree. In their efforts to maintain a standardized image and marketing approach to the general buying public, the franchisors usually retain a strong, formalized system of control of the business operation. In this type of franchise, the responsibilities of both parties—franchisor and franchisee—are spelled out in the franchise contract, and are usually considered to be of mutual advantage to both parties.

How Franchising Works

The franchise system may be used for either goods or services. Although most franchise businesses are in consumer lines, some involve industrial goods and services. In any case, however, they work in generally the same manner. The purchaser of the franchise—the franchisee—is an independent businessman who contracts for a "package" business.

Normally, this contract obligates the businessman to some combination of the following:

1. To make a minimum investment of money

2. To obtain and maintain a standardized inventory and/or equipment package

3. To maintain a specified quality level of performance

USUAL FRANCHISEE CONTRACT OBLIGATIONS

To

1. MAKE A MINIMUM FINANCIAL INVESTMENT
2. ACQUIRE STANDARDIZED INVENTORY AND EQUIPMENT
3. MAINTAIN A QUALITY PERFORMANCE LEVEL
4. FOLLOW SPECIFIED PROCEDURES
5. PAY FRANCHISE FEES
6. MAINTAIN A CONTINUING BUSINESS RELATIONSHIP

Visual 4

BASIC FRANCHISOR GUARANTEES

1. USE OF COMPANY NAME
2. USE OF IDENTIFYING SYMBOLS AND DESIGNS
3. MANAGEMENT AND EMPLOYEE TRAINING
4. WHOLESALE PRICES ON MERCHANDISE
5. FINANCIAL ASSISTANCE
6. CONTINUING AID AND GUIDANCE

Visual 5

Visual 6

4. To follow specified operating procedures and the promotional efforts of the parent firm
5. To pay royalty or franchise fees
6. To engage in a continuing business relationship

While this may seem excessively binding upon the franchisee, the franchise contract usually puts a similar responsibility on the franchisor.

The franchisor usually guarantees the franchisee some combination of these elements:

1. Use of the company name
2. Use of identifying symbols, designs, and facilities
3. Professional management and employee training
4. Wholesale prices on specific merchandise
5. Financial assistance (of various types)
6. Continuing aid and guidance

Why Franchising Works

The reason that franchising works can be summed up in one six-letter word—PROFIT! The parent company earns its money through the continuing success of its franchises. For this reason, franchisors constantly continue to assist their franchisees with training, promotion, advertising, and new product development, and generally assist with any problems that crop up.

The franchisee has the advantage of a "proven" business formula, and is literally led by the hand to success in his venture.

ADVANTAGES OF FRANCHISING

The trend toward franchising of business activity is continuing. The system combines much of the corporate strength and efficiency of big business, while capitalizing on individual business drive and motivation to capture fully 10 percent of the Gross National Product.

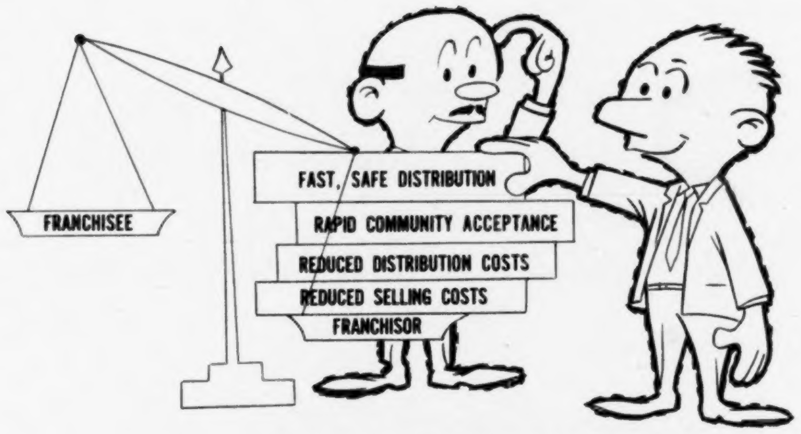
Advantages to Franchisor

To a franchisor, a franchise permits a fast, efficient, and reasonably safe method to achieve wide distribution without large capital expenditures. He knows that the financial investment of the franchisee will create a stronger motivation to perform effectively than would be available from a manager.

He assures himself of faster community acceptance because of the local management-ownership.

The franchisor's costs are reduced for a given volume of distribution because the franchisee bears part of them as a cost of doing business.

Selling costs are reduced because of the captive market (the franchisees).


FRANCHISEE
FAST, SAFE DISTRIBUTION
RAPID COMMUNITY ACCEPTANCE
REDUCED DISTRIBUTION COSTS
REDUCED SELLING COSTS
FRANCHISOR

ADVANTAGES TO FRANCHISOR

Visual 7

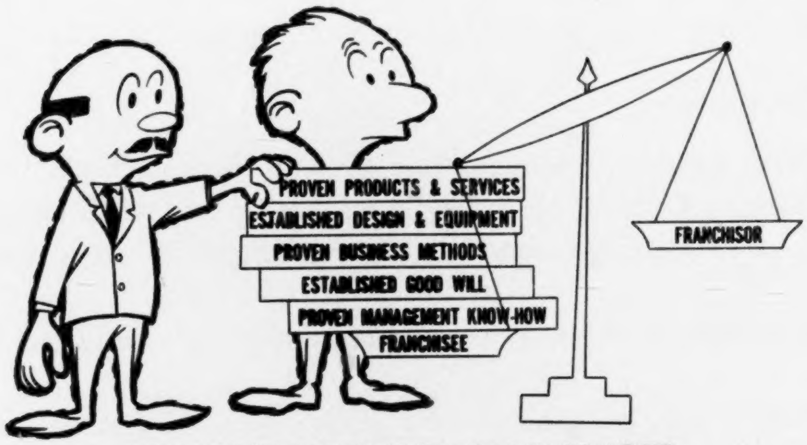
Advantages to Franchisee

The franchisee, unless he is lacking the basic skills, education, or personality to ever succeed, can step right into business with a minimum of previous experience, a relatively small amount of capital, and have a good possibility of succeeding in his venture because of the franchisor's experience, knowledge, and support.

The franchisee can normally expect to be trained in the mechanics of the business, and guided in the day-to-day operation until he is proficient at the job. Moreover, management consultant service is provided by the franchisor on a continuing basis.

He is buying a "success" package, where all of the headaches of development work in preparing a consumer-accepted image, establishing goodwill, designing fixtures, and perfecting handling methods have been done for him. Included in this package are proven and well-known products and services.

Another advantage of franchising to the franchisee is that he obtains more standing with financial institutions and credit associations.


PROVEN PRODUCTS & SERVICES
ESTABLISHED DESIGN & EQUIPMENT
PROVEN BUSINESS METHODS
ESTABLISHED GOOD WILL
PROVEN MANAGEMENT KNOW-HOW
FRANCHISEE
FRANCHISOR

ADVANTAGES TO FRANCHISEE

Visual 8

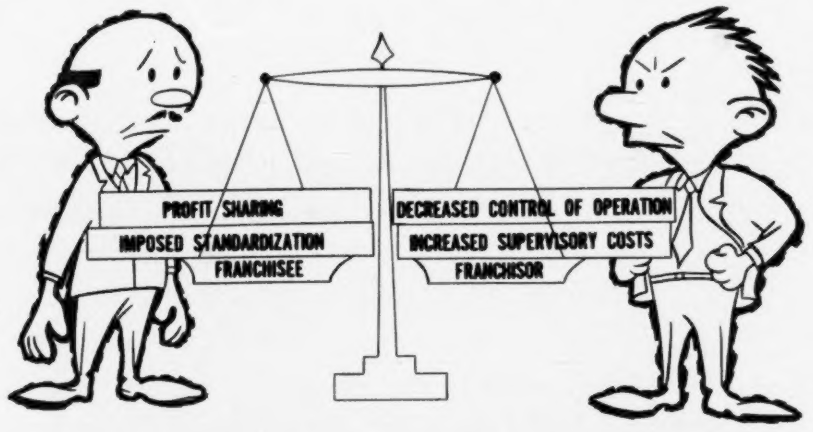
The franchisee generally has a favorable income potential and a *lower* risk of failure than if he tried to develop a similiar business completely on his own. Over 90 percent of new franchising businesses flourish, compared with approximately 13 percent of all new business starts which succeed.*

DISADVANTAGES OF FRANCHISING

At this point, franchising no doubt sounds like a 20th century utopia—the answer to everyone's problems. There *are* disadvantages, and they should not be overlooked.

Disadvantages to Franchisor

To the franchisor, there is a certain loss of control of the operation. Franchisees are—quite understandably—more independent than salaried managers would be. So the franchisor's supervisory costs are higher as he tries to insure standardized operations by his various franchisees.



DISADVANTAGES OF FRANCHISING

Visual 9

Franchisors must wage a constant battle against the desire of their francisees to add "foreign" products to their individual operations, plan their own promotions, and depart from the standards set up by the parent firm.

Disadvantages to Franchisee

The franchisee, on the other hand, faces other disadvantages. He must share the income from the business in some manner with the franchisor, whether in the form of a percent of gross sales, a markup on supplies, a flat annual fee, or a combination of these.

He must also accept a certain amount of control over his method of operation, agree to handle a product or products that may not be particularly profitable in his marketing area, or otherwise be subject to certain policies and business practices that benefit others in the chain, but may be injurious to him.

**"Building Your Future Through Franchising" issued by The International Franchise Association.*

WHERE TO FIND FRANCHISE OPPORTUNITIES

Well, now that we know what franchising is, how and why it works, and some of the advantages and disadvantages, how can we go about finding the right franchise opportunity?

There are a number of good sources of information for franchise offers. Here is a list of six of the most important:

1. Annual directories
2. Daily newspapers
3. Trade publications
4. Franchising publications
5. Franchisor exhibitions
6. Franchise marketing agencies

Annual Directories

Two comprehensive directories of franchising companies are published annually. One is "The Franchise Annual", prepared by National Franchise Reports, 333 No. Michigan Avenue, Chicago, Ill. 60601. The other is "Directory of Franchising Organizations and A Guide to Franchising", published by Pilot Industries, Inc., 42 West 33d Street, New York, N.Y. 10001.

Daily Newspapers

The classified sections of most daily metropolitan newspapers carry franchise opportunities under the "Business Opportunities" heading. It is not unusual for the franchisor to run what is termed a "blind ad", giving no name, but listing a box number for the prospective applicant to write to. This practice enables the franchisor to accomplish a preliminary screening and eliminate the "shoppers" from the "buyers."

Trade Publications

Many companies seek franchisees through advertisements placed in trade publications that are related to the franchised business. Public libraries in most large cities subscribe to a variety of these trade magazines, and are an excellent place for the prospective franchisee to seek an opportunity in the field that interests him.

Franchising Publications

Publications devoted strictly to franchising are another excellent source of information. "National Franchise Reports", mentioned a minute ago, publishes a monthly newsletter with the same name, sold by subscription, which is considered by many authorities to be the "bible" of franchising. This publication reports the details of new franchise offers in each issue, lists the current franchise shows, and generally contains some editorial comment by the publisher.

"Modern Franchising", 1033 First Avenue, Des Plaines, Ill. 60016, is a bimonthly news and information magazine aimed at prospective franchisees. Advertisements in the magazine are an excellent source of franchise offers.

Other magazines such as "Income Opportunities", carry feature stories concerning franchising, and a number of advertisements by franchisors.

The Boston College Center for the Study of Franchise Distribution has a collection of written materials on franchising. (NOTE: Additional sources of information are listed in the Bibliography.)

Franchisor Exhibitions

Franchisor exhibitions are held in major cities all over the Nation, and offer the prospective franchisee the opportunity to meet "face-to-face" with franchisor representatives, and evaluate a number of offers in one visit. A good source of information on the schedule of these exhibitions is the International Franchise Association, 549 West Randolph Street, Chicago, Ill. 60606.

Franchise Marketing Agencies

Franchise marketing agencies and franchise consultants, while relatively new to the industry, show prospects of being an important link in the growth of franchising. A list of franchise consultants is available in "The Franchise Boom", a publication prepared by Harry Kurch and published by Prentice-Hall, Inc., Englewood Cliffs, N.J. 07632.

SOURCES OF FRANCHISE OPPORTUNITY INFORMATION

1. **ANNUAL DIRECTORIES**
2. **DAILY NEWSPAPERS**
3. **TRADE PUBLICATIONS**
4. **FRANCHISING PUBLICATIONS**
5. **FRANCHISOR EXHIBITIONS**
6. **FRANCHISE MARKETING AGENCIES**

Visual 10

EVALUATING A FRANCHISE OPPORTUNITY

A franchise can be purchased for as *little* as a few hundreds dollars, or as *much* as a quarter of a million dollars or more. With this dollar spread, and the fact that there are *thousands* of franchises to choose from, it can be difficult for the prospective franchisee to make a selection. But, by being systematic in evaluation, a lot of confusion can be eliminated.

Investigate Before Investing

A simple rule, and yet an important one is, simply: "Investigate *before* investing". Many of the so-called "fast-buck" artists peddling worthless franchise offers for an attractive low price, prey on the unwary. The parent company in such deals normally doesn't care about the continuity of the franchise—their profit is made from wholesale peddling of the franchises. The investor seldom can recover *any* of his money, and he has had an expensive lesson.

An effective way to begin is to ask the franchising company for a list of existing franchises in the area *you* are considering. From it, you can select several locations, and visit them during business hours.

By spending some time at each of the franchise operations, you can make many important observations for yourself:

How much traffic does the store have? What are the buying patterns of its customers? Are they shopping? Or buying?

Don't hesitate to ask the franchisees about the business. Most legitimate franchisors encourage their franchisees to answer frankly *all* questions put to them by any prospective investors. And the information you obtain can be valuable in guiding your own decision.

Investigate the company. With the preliminaries behind you, and your interest still high, the next step is to investigate the company who is offering the franchise.

How long has the firm been in operation in the particular field you are interested in? While there are many "young" firms that offer very worthwhile franchises, the length of time in business is still an effective measuring stick.

What is the financial position of the franchisor? Who do they offer—particularly financial institutions—as references? You can then discuss their listings with your local bank, your Chamber of Commerce, and the Better Business Bureau. Check with Dun & Bradstreet.

Examine the firm's plans for future development. This is an important factor, and can influence the future value of your franchise. So don't overlook it.

How "choosy" is the franchisor in awarding his license? Normally, the franchise has more intrinsic *value* if you have to work to get it. If it is awarded too easily, then anyone can get one, and the resale value of *your* franchise can plummet down to a fraction of your initial investment.

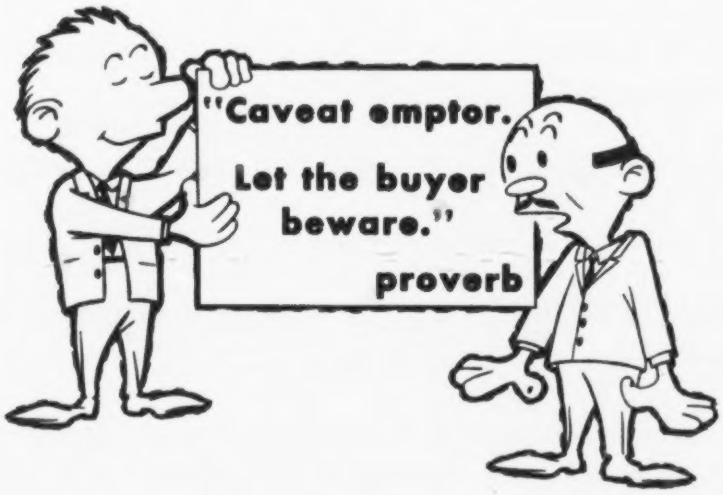
The International Franchise Association (IFA)* and the Federal Trade Commission have repeatedly cautioned against a number of operators who, by their practices, are damaging to franchising.

A carefully drawn list of what you as a prospective franchisee should watch out for would include franchisors—

- Who grossly exaggerate potential earnings to attract franchisees.
- Whose costs for equipment and supplies are outrageously high.
- Whose royalty or other financing charges are exorbitantly out of proportion to sales volume.
- Who have a record of business failures.
- Whose selection of new sites is haphazard.

**IFA, as the official organization representing the franchise industry, is a good source for checking a company making a franchise offer.*

- Whose agreements do not allow the franchisee freedom to make basic decisions.
- Who give certain franchisees preferential treatment.
- Whose real business is only in *selling* franchises.
- Who deceptively minimize the cost of doing business.
- Who accept as franchisees persons lacking the basic skills, education, or personality to ever succeed.
- Who fail to provide proper training and continuing supervision.


"Caveat emptor.
Let the buyer beware."
proverb

Visual 11

Investigate the product. Let's assume that the company has stood up under your careful scrutiny. What about the product that you will handle in the operation of your franchised business?

Is the product a staple? Will it bring repeat business? Or is it a luxury item? If it is seasonal, will you be able to survive the long "slow" periods between peak selling months? How well is it selling on the present market?

Is it of good quality? Would *you* purchase it, of your own volition, from another vendor?

How many competing products are of comparable quality? Of better quality? Of more attractive price?

Where else is the product being sold? Will you be handling an "exclusive"?

Investigate the territory. This naturally leads us into a thorough study of the marketing area for your franchise. You must consider the trading area from which you will pull customers, and the geographical limits of your franchise.

How well is your territory defined? Will it support a sales volume adequate to meet your projected costs and profit requirement? Is there adequate room for sales growth? What is the *present* market penetration by other franchisees?

How effective is competition in your proposed territory? Can competition grow without "crowding" *your* proposed market?

Investigate the contract. By this time in your investigation, you will probably have availed yourself of sound legal counsel. If you have not, by all means, do so *before* you attempt to evaluate the franchise contract. The small investment in an attorney at this stage of the game can save enormous sums of money later on. The contract, once signed by both parties, is a legal binding document. Any misunderstanding in contract content can be expensive—and seldom for the franchisor. The time to determine the strengths and weaknesses of the contract is BEFORE signing it.

In examining the contract, some of the key points to evaluate are:

- Does the contract cover all of the material discussed in any preliminary discussions?
- Can the contract be renewed, transferred, or terminated? Is there a time limit involved? How can it be terminated?
- What are the total financial considerations in the contract?
- Are there any sales quotas involved? Merchandise purchase quotas? Will financial penalties be invoked in the event of missed quotas?
- What are the restrictions on other business activities by the franchisee?
- What limitations are imposed on the size of the franchise operation?

Of course, it would be impossible to list all possible considerations in contract analysis—another good reason to seek out competent legal counsel.

Investigate continuing assistance. Still another measure of the value of a franchise is the willingness of the franchisor to provide continuing assistance. Naturally, the prospective investor should determine the type and amount of assistance to expect. Will the franchisor provide initial training for the franchisee and key employees? How about new employees as the operation grows? Will the franchisor supply sales kits, manuals, and business forms? Does the parent company offer financial assistance? To what extent? What is the advertising and promotion policy of the company? Will the franchisee have to share in the costs? On what basis? Will the franchisor assist in the analysis of financial statements? How about continuing market surveys?

Control as a Mutual Exchange of Values

Finally, just how much control will the franchisor maintain over the business operation? A manufacturer or distributor licenses franchisees because he is aware of the opportunity to trade his proven experience and known product acceptance for the investor's money and time. However, the franchisee is an individual, independent businessman, who often tends to veer off in his own direction once he has been trained in the mechanics of the business. Therefore, a franchisor tries to use a contract which contains rules which afford adequate control *without* stifling the individuality of the franchisee. But the amount of control varies with the individual franchise opportunity, and must be taken into consideration early in the evaluation. It should be based on a mutual exchange of values between the franchisor and the franchisee involved. (NOTE: Pass out copies of the checklist for *Evaluating A Franchise* from The Supply Department section of this booklet.)

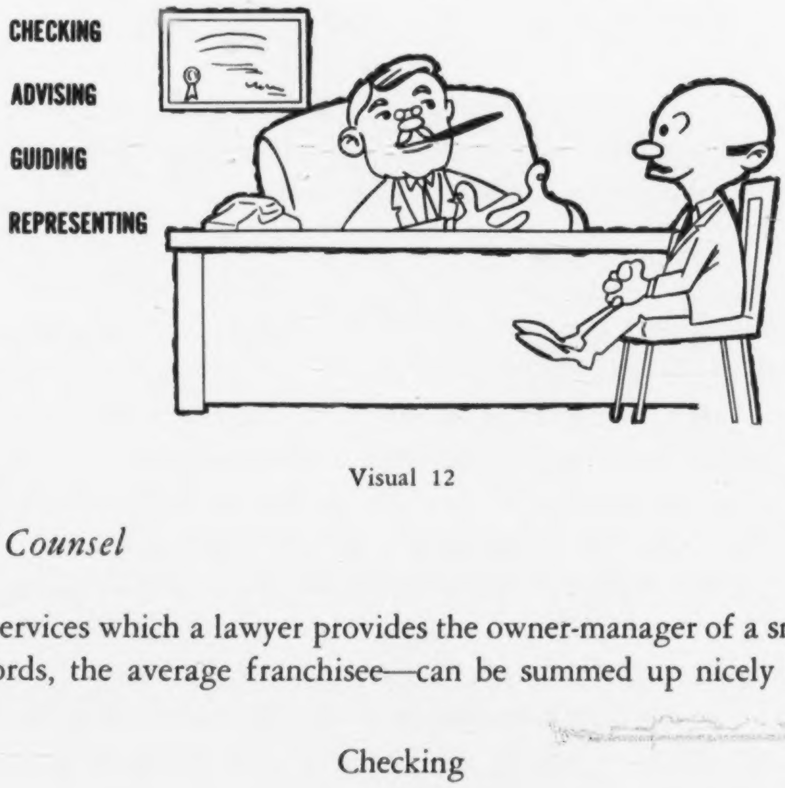
LEGAL COUNSELLING

The operation of any business, large or small, cuts across legal principles applicable to the rights of both buyers and sellers, to landlords and tenants, creditors and debtors, employers and employees, and many other groups in a competitive economy and a mobile society.

Need for Legal Counsel

Many small business owners consider legal services *only* when their firms are actually in trouble. They fail to appreciate the fact that legal trouble can be reduced and in many cases *avoided* by a program of consultation which is carried out on a continuing basis. The advice and suggestions of a lawyer on day-to-day operations help prevent costly and time-consuming problems.

SERVICES OF LEGAL COUNSEL



Visual 12

Services of Legal Counsel

The legal services which a lawyer provides the owner-manager of a small retail or service firm—in other words, the average franchisee—can be summed up nicely in four key words:

Checking

Advising

Guiding

Representing

Your own lawyer can *check* past actions to determine if you have unintentionally violated the law. He can assist you in your continuing relationship with your franchisor. He can see to it that all the obligations affecting both parties in the contract are adhered to, to gain maximum benefit for you, and to prevent any damage action by the franchisor for nonperformance by you.

In *advising,* the lawyer can explain the legal principles involved in the various courses of action which are open to you under the law. A decision will be simple, of course, when the law allows only one course of legal action. But making the decision when there are several lines of action open to the franchisee can be difficult.

This is where a lawyer's *guidance* can be extremely valuable. While the ultimate decision is the responsibility of the franchisee, the lawyer can help evaluate the courses of action and can materially assist in making the final decision.

In *representing* the franchisee, the lawyer speaks as one specialist to other specialists. He knows the language of licensing boards, regulatory bodies, and other governmental agencies. And he is at all times protecting your interests in negotiating and drawing up contracts, interpreting restrictive clauses, and otherwise helping prevent costly and time-consuming problems. His counsel will be particularly valuable in obtaining financial assistance to begin and operate your business.

FINANCIAL ASSISTANCE

A characteristic of franchise businesses is that the financial investment required is usually *less* than for a similar business begun completely independently. And the actual cash investment represents only a fraction of the actual business worth.

Capital Requirements

One study indicates that the average cash requirement for a franchise applicant ranges from just over $4,000 to about $6,500. But of course, an average is just that. Some types of franchises can be purchased for an investment as low as a few hundred dollars, while others have been known to require in excess of $200,000. The variations spring largely from the type of business that the investor is considering. And even in the same line of business, there are variations that reflect the scale of operations available to the franchisee.

The prudent investor will soon discover that he must consider his total capital requirement, and look beyond the initial advertised capital investment. He must provide for operating capital to enable him to survive the "rough" months of early business activity, while his income is sporadic. In many cases, the franchisor has "come to the rescue" of an earnest, hard-working franchisee in temporary financial trouble. But the investor deciding to go into business cannot count on it. He should provide for his necessary capital before he begins operations.

Lending Institutions

There are many ways to raise money through borrowing. Probably the most common source of borrowed money for franchised businesses is from friends and relatives. In fact, the practice is so common that many franchise companies provide financial data to the prospective franchisee to help him convince his lenders of the potential business opportunity.

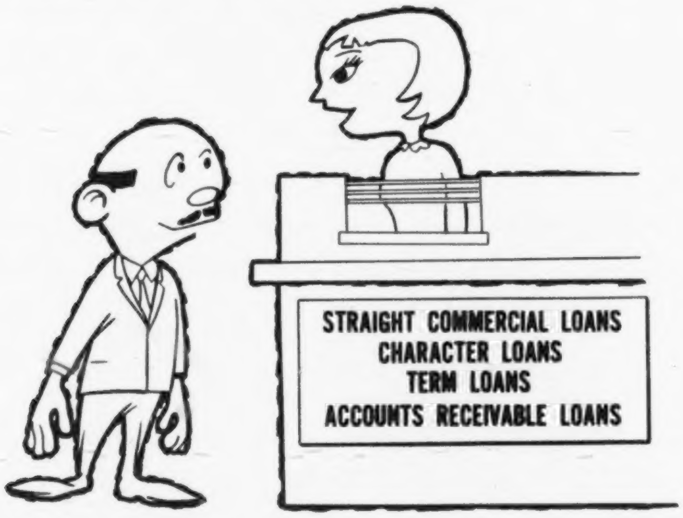
BANKS: Types of Loans. The local bank is one of the best sources for investment capital. Not only is it valuable as a source of money, but by keeping its finger on the pulse of the business community, the local bank can offer valuable advice on regional conditions, community attitudes, and the business experience of other franchisees in the area.

It is important for the prospective investor to realize that there are a number of types of loans available to him. Principal types of bank loans available are:

STRAIGHT COMMERCIAL LOANS, usually made for a period ranging from 30 to 90 days. These loans are usually made on the strength of the financial statements of the borrower, and are self-liquidating. This type of loan is commonly used for seasonal financing.

CHARACTER LOANS, usually of the consumer credit variety, but nevertheless often used for business—particularly by the small firm.

TYPES OF BANK LOANS



Visual 13

TERM LOANS, having a maturity of from 1 to 10 years. They may be secured or unsecured. Repayments are on a specific schedule, varying from monthly to annually.

COLLATERAL LOANS, made on certain securities and accounts receivable. The security can take the form of real estate mortgages, cash surrender values of life insurance policies, and stocks and bonds.

Banks can also help you raise capital by buying from you the installment credit contracts of your customers. Of course, this presupposes that your business is the type that justifies such activity by the bank. In many cases, if the banker himself is unable to meet your capital needs, he can direct you to another source of funds. (NOTE: Refer to handout, "The ABC's of Borrowing".)

Veterans Administration. The Veterans Administration is still active in aiding GIs to obtain loans for starting and running a business. The VA is also a comprehensive source of business advice, with wide experience in aiding GIs to solve business problems.

Small Business Administration. The Small Business Administration has field offices strategically located throughout the United States. This agency of the Federal Government is a cosponsor of this management education program. One of its major responsibilities is to help small business concerns meet their capital needs.

An essential part of the assistance SBA offers small-businessmen is counselling by financial experts. Sometimes, an SBA specialist can show a businessman that borrowing is inadvisable or unnecessary. If borrowing does appear to be the answer to the small-business owner's problem, SBA may be able to help him obtain a bank loan or other private financing.

SBA maintains a comprehensive program of financial assistance, designed to help the new businessman as well as the established firm in need of additional funding.

The importance of franchising is recognized in action taken by the SBA to make qualified franchisees eligible for loans.*

MANAGEMENT AND TECHNICAL AID

The typical franchisee has had little or no experience in the field of the franchise, and leans heavily on the franchisor for management and technical aid, particularly during the early months of business operation. The franchisor, eager to insure a successful operation, finds it quite desirable to be able to spell out various operating procedures rather precisely. In a sense, this is a form of control, but it furnishes the best way of obtaining satisfactory performance from a group of franchisees of varying backgrounds, skills, aptitudes, and attitudes.

This aid by the franchisor affords a degree of standardization throughout the system, and enables the individual franchisee to benefit from the experience of the franchisor and other franchisees.

Franchisor guidance often begins at the outset of the venture, when the franchisee is hunting a location. In fact, so important is location for many types of franchise operation that franchisor approval for the site is often part of the franchise agreement. The amount of aid offered by the parent firm varies from a simple checklist of things to look for to a complete town survey, including a detailed analysis of retail trade, population studies, and even a comparison of the town with a standard norm.

Many franchisors have developed efficient and attractive building designs and floor layouts, especially for retail installations.

It is common practice to make available to the franchisee a complete "package" of fixtures and equipment, often with operating supplies and advertising materials.

Many franchisors offer a basic package which provides the minimum equipment necessary to begin a business. The franchisee can purchase either auxiliary equipment or a more elaborate package if he desires it.

Promotional Support

The franchisee can turn to his franchisor for promotional support, both on a contributory and noncontributory basis. Many franchisors centrally prepare a complete promotional campaign, including direct-mail material, point-of-sale display material and signs, highway signs, leaflets, handbills, newspaper mats, and house organs. The franchisee avails himself of all or part of this valuable material as he requires it. Some franchisors carry this service a step further and actually prepare a promotional schedule which suggests the specific material to be used, the media to use it in, and the seasonal timing for most effective use of the material.

**References to franchising and the SBA, include:*

1. *SBA Press Release, Sept. 9, 1966.*
2. *Talk by Philip F. Ziedman, SBA General Council, in Cleveland, Sept. 9, 1966.*
3. *Talk by John E. Horne, annual meeting of IFA, Feb. 8, 1963.*

Recordkeeping Systems

The support that a franchisee may receive extends even to accounting and inventory control systems, developed by the franchisor to cover all contingencies. Many of the franchising companies have hired top experts in the country to develop these systems, and they permit the individual operator to keep himself constantly abreast of his financial position.

Training Programs for Franchisees

Since the typical franchisee has no experience in the type of business he is entering, he is usually in need of some training. Virtually all franchisors attempt to train their new franchisees. The training programs vary from a few days of supervision to several weeks of intensive classroom training supplemented by on-the-job activity at the site of an established franchise operation.

Refresher training courses are another important service now appearing in many franchising programs. This program of retraining varies from 1-day seminars at the home office of the franchisor to field-located sessions conducted by traveling supervisors. But it is an indication of the technical aid given by the progressive franchisors to better support their franchisees.

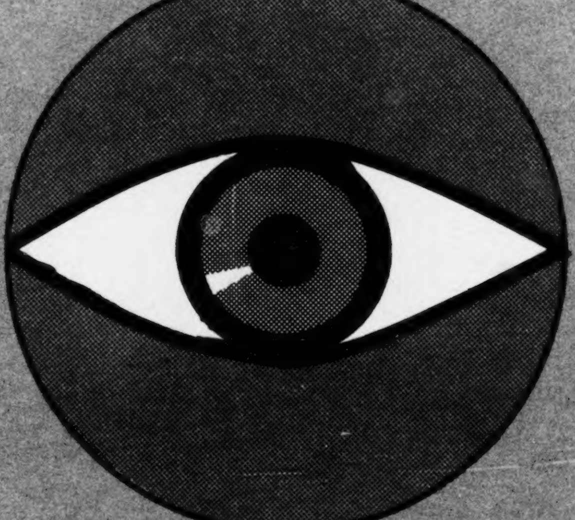
SUMMARY

The continuing growth of franchising is apparently in a direct parallel with the economic and social trends of more leisure time and the willingness to purchase services, recreational activities, and education.

Franchises that presently provide some of the best opportunities are those that cater to the "luxury" needs—travel, entertainment, reading, sports, beauty care, home services, cleaning and pressing—the services that make life easier, more enjoyable, and happier.

The small business franchise is directly tied to the trend of the latest economic phenomenon—the spending habits of the American consumer. Thousands of enterprising investors have taken the franchised road to independence and personal fortune through businesses of their own.

The outlook for franchising is now more impressive than *ever before* in our economic history.



THE VISUAL AIDS

A What to Show

Section

The old Chinese proverb **"One See Worth Thousand Say"** is certainly borne out by experience in the fields of education and training at all levels.

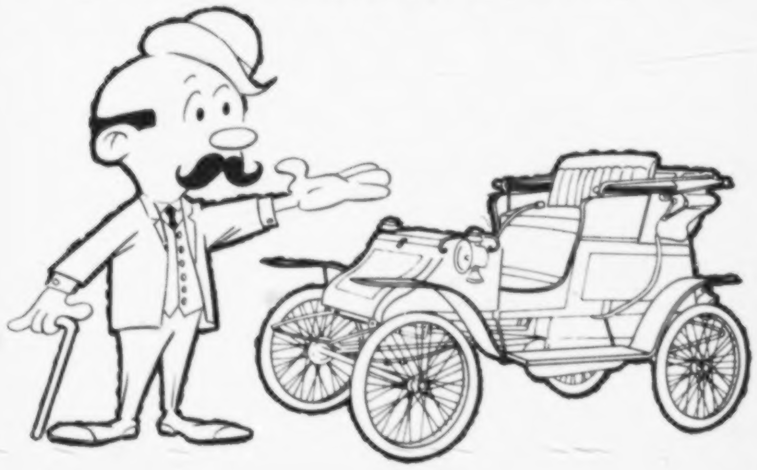
The instructor who helps his participants visualize subject matter and ideas not only holds the group interest--he also stimulates thoughtful consideration and retention of the topic.

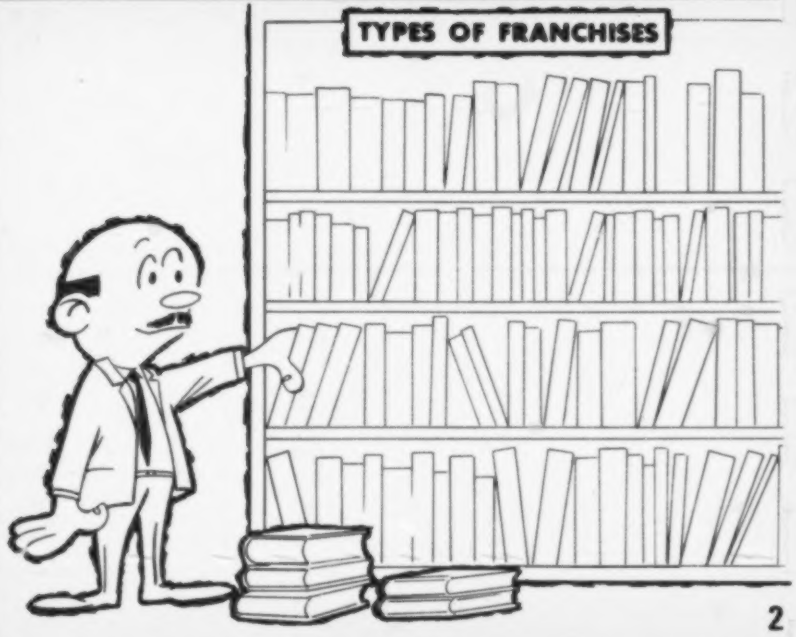
This section contains samples of visuals that are available for this subject. Each has been carefully coded and "keyed" into **The Lesson Plan** as outlined in this manual.

USE OF VISUAL AIDS

WHAT TO USE	WHEN AND HOW TO USE
Chalkboard 	Study and plan before a meeting what to put on the board and where to put it. Use it to present sketches, diagrams, outlines, definitions, key words, directions, record of class contributions, and summaries. Suit material to board space. Write plainly and quickly. Keep wording simple. Stand at one side of board while referring to material. Talk to the group, not to the board. Erase material no longer needed.
Posters, Charts, and Diagrams 	To arouse interest and attract attention; to show relationships and trends; to inspire group. Use device large enough to be seen. Post where everyone can see. Present at right time. Discuss information illustrated.
Hand-Out Materials 	To present information uniform in character and as a guide to material covered; emphasize key points; arouse interest and discussion; review or summarize discussions; and serve as permanent reference. Select to serve a definite purpose. Introduce at right time. Distribute in manner to convey its importance. Direct members how to use.
Films and Film Strips 	Present an overall view; introduce a new subject; emphasize specific aspects of a subject; arouse interest; summarize. Select carefully to relate to the discussion and plan presentation. Arrange room and equipment for showing. Alert the audience for the showing or what will be seen. Run the film. Discuss the subject matter and summarize.
Samples, Forms, and Exhibits It's the BEST	Keep subject matter practical; show development of a process; increase understanding. Select only enough to illustrate, not confuse. Pass around if necessary. Take time to present clearly. Comment when presenting.
Pedestal Chart MAKE it Count	A pad of newsprint sheets or similar paper may be used for the same purposes as the chalkboard. Material recorded with chalk or crayon may be saved for future reference by the group or by the instructor.

EARLY FRANCHISE BUSINESS





DEFINITION OF FRANCHISING

FRANCHISING IS THE SYSTEM OF DISTRIBUTION WHICH ENABLES A SUPPLIER (FRANCHISOR) TO ARRANGE FOR A DEALER (FRANCHISEE) TO HANDLE HIS PRODUCT OR SERVICE UNDER CERTAIN MUTUALLY AGREED UPON CONDITIONS.

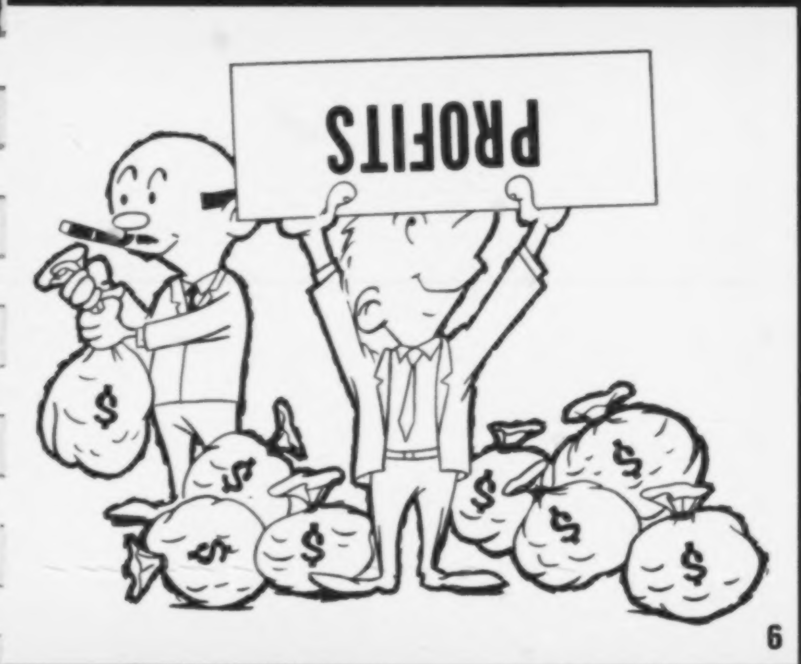
USUAL FRANCHISEE CONTRACT OBLIGATIONS

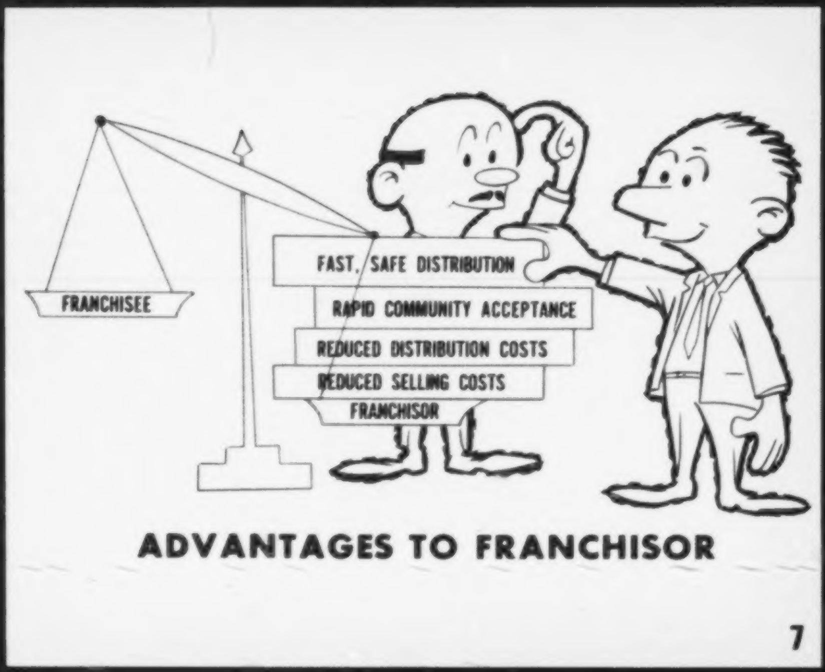
To

1. MAKE A MINIMUM FINANCIAL INVESTMENT
2. ACQUIRE STANDARDIZED INVENTORY AND EQUIPMENT
3. MAINTAIN A QUALITY PERFORMANCE LEVEL
4. FOLLOW SPECIFIED PROCEDURES
5. PAY FRANCHISE FEES
6. MAINTAIN A CONTINUING BUSINESS RELATIONSHIP

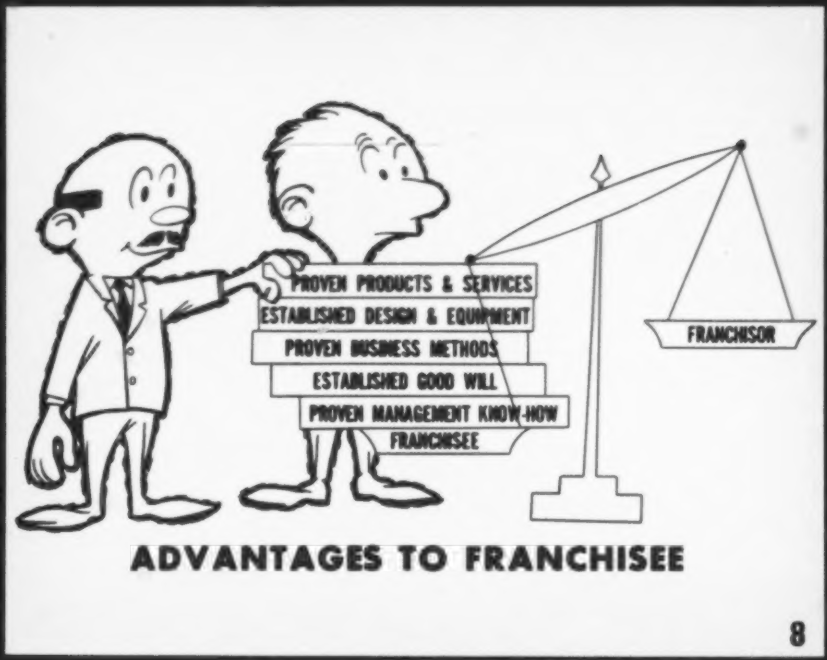
BASIC FRANCHISOR GUARANTEES

1. USE OF COMPANY NAME
2. USE OF IDENTIFYING SYMBOLS AND DESIGNS
3. MANAGEMENT AND EMPLOYEE TRAINING
4. WHOLESALE PRICES ON MERCHANDISE
5. FINANCIAL ASSISTANCE
6. CONTINUING AID AND GUIDANCE

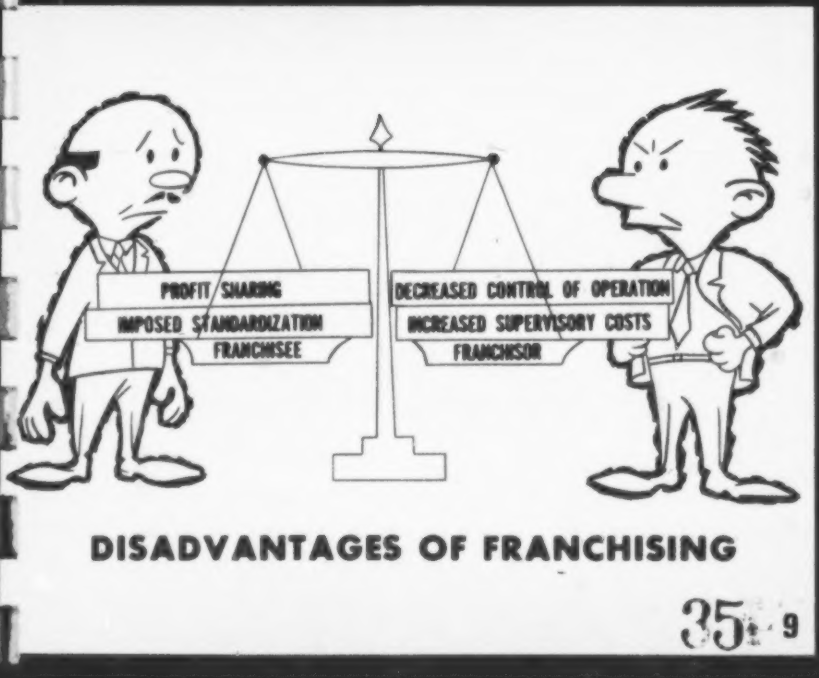



FRANCHISEE
FAST, SAFE DISTRIBUTION
RAPID COMMUNITY ACCEPTANCE
REDUCED DISTRIBUTION COSTS
REDUCED SELLING COSTS
FRANCHISOR
7

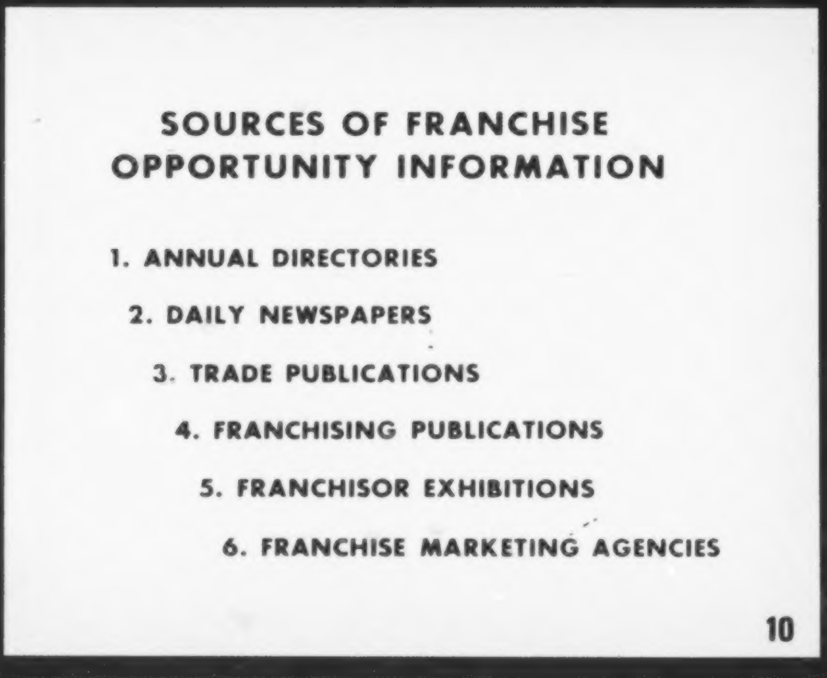
ADVANTAGES TO FRANCHISOR


PROVEN PRODUCTS & SERVICES
ESTABLISHED DESIGN & EQUIPMENT
PROVEN BUSINESS METHODS
ESTABLISHED GOOD WILL
PROVEN MANAGEMENT KNOW-HOW
FRANCHISEE
FRANCHISOR
8

ADVANTAGES TO FRANCHISEE

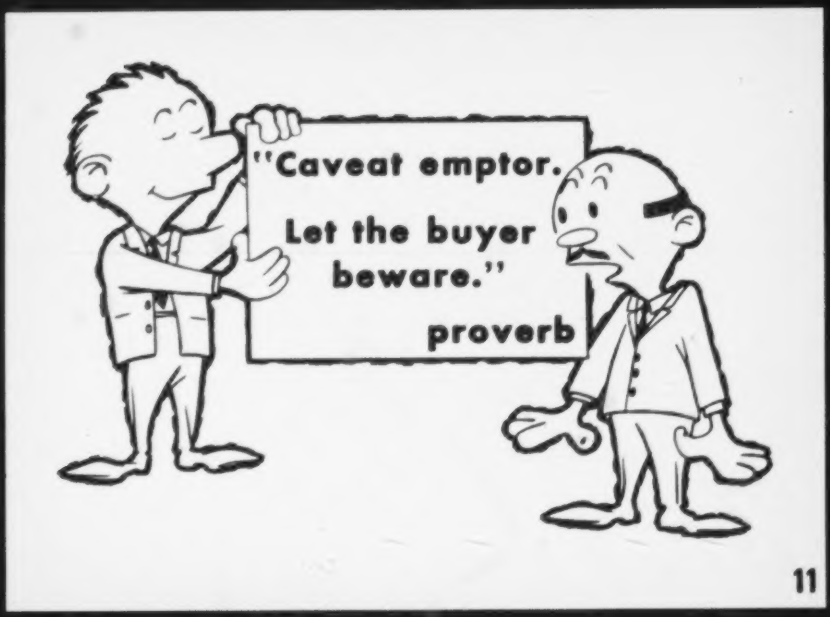

PROFIT SHARING
IMPOSED STANDARDIZATION
FRANCHISEE
DECREASED CONTROL OF OPERATION
INCREASED SUPERVISORY COSTS
FRANCHISOR
35
9

DISADVANTAGES OF FRANCHISING

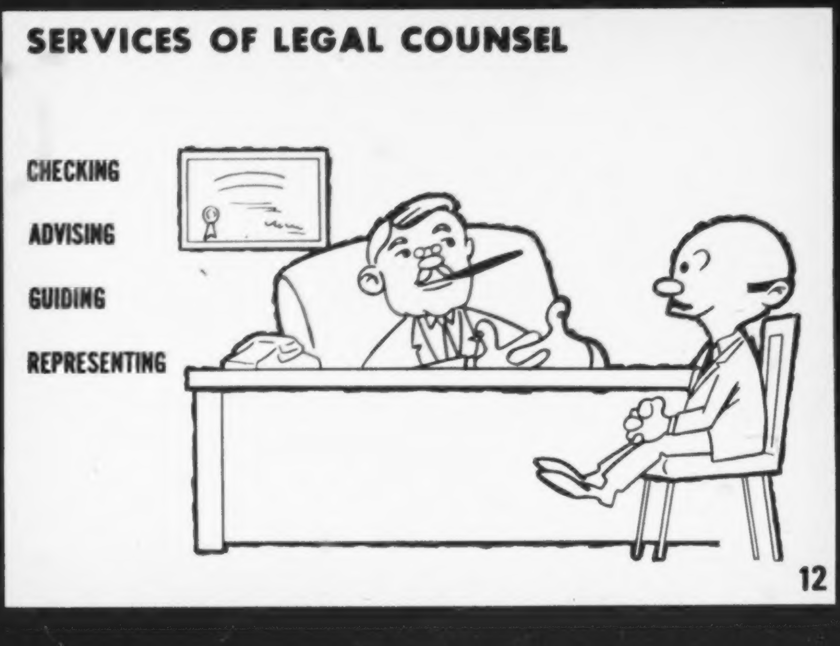


SOURCES OF FRANCHISE OPPORTUNITY INFORMATION

1. ANNUAL DIRECTORIES
2. DAILY NEWSPAPERS
3. TRADE PUBLICATIONS
4. FRANCHISING PUBLICATIONS
5. FRANCHISOR EXHIBITIONS
6. FRANCHISE MARKETING AGENCIES


"Caveat emptor.
Let the buyer beware."
proverb

11



SERVICES OF LEGAL COUNSEL

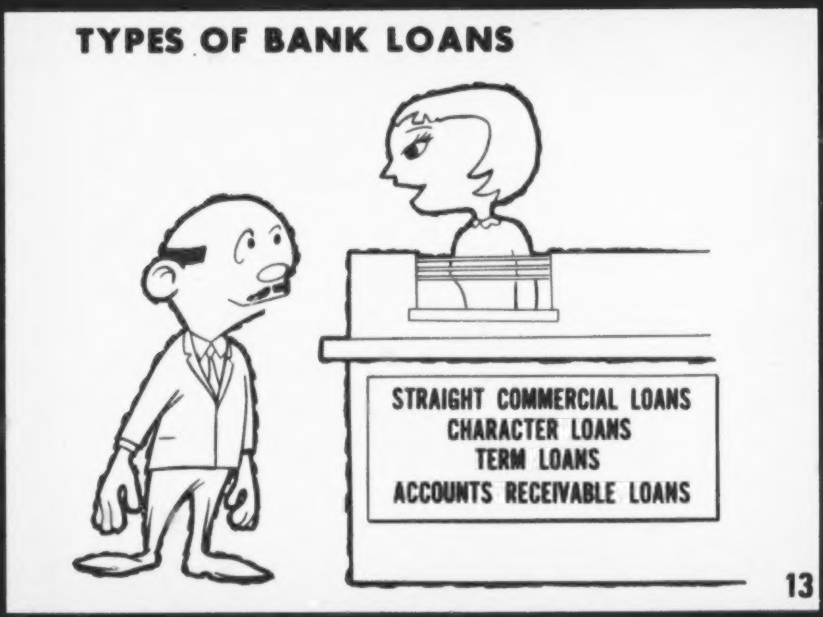
CHECKING

ADVISING

GUIDING

REPRESENTING

12



TYPES OF BANK LOANS

STRAIGHT COMMERCIAL LOANS
CHARACTER LOANS
TERM LOANS
ACCOUNTS RECEIVABLE LOANS

13

TRAINING AIDS
MANAGEMENT AIDS
MENT AID
HOW TO MANAGE
TIONS
TRAINING AID

THE SUPPLY DEPARTMENT

A Resource Materials and Participant Handout

Section

It is generally conceded that interest intensifies in situations where people have a chance "to participate" by such means as open discussion and buzz sessions. The materials in this section should prove useful in this kind of activity. These materials may be reproduced locally.

It is also desirable to provide participants with "take away" materials if they are pertinent and concise. Accordingly, appropriate Management Aids, Small Marketers Aids, and Management Research Summaries are included in this section. Current information on the availability of suggested and new SBA publications may be obtained from the nearest SBA office.

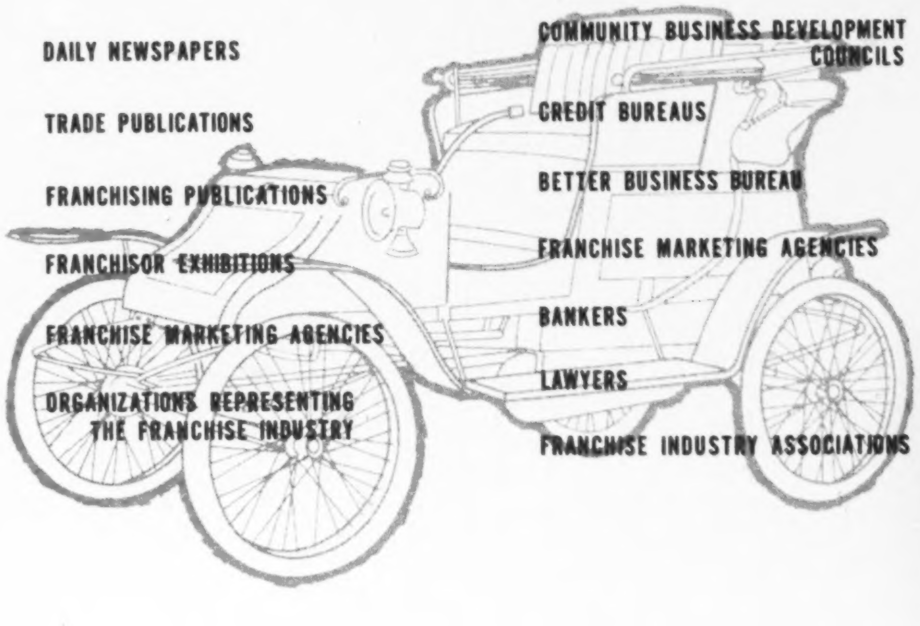
LIST OF HANDOUT MATERIAL

1. Focal Points (brochure). Order quantity needed from SBA.
2. Evaluating A Franchise.
3. SMA #71, Checklist for Going Into Business.
4. SMA #115, Are You Ready for Franchising?
5. MRS #172, The Franchise System of Distribution.
6. Management Aid #170, The ABC's of Borrowing.
7. Management Aid #182, Expanding Sales Through Franchising.
8. Counseling Notes #3, Franchised Businesses.
9. Changing Times, the New Look in Franchising.
10. The Bibliography is intended primarily for use by the instructor but may also be duplicated and utilized as a helpful handout item.

WHAT TO WATCH OUT FOR IN A FRANCHISOR

FRANCHISORS:

1. WHO GROSSLY EXAGGERATE POTENTIAL EARNINGS TO ATTRACT FRANCHISEES
2. WHOSE COSTS FOR EQUIPMENT AND SUPPLIES ARE OUTRAGEOUSLY HIGH
3. WHOSE ROYALTY OR OTHER FINANCING CHARGES ARE EXHORBITANTLY OUT OF PROPORTION TO SALES VOLUME
4. WITH A RECORD OF BUSINESS FAILURES
5. WHOSE SELECTION OF NEW SITES IS HAPHAZARD
6. WHOSE AGREEMENTS DO NOT ALLOW THE FRANCHISEE FREEDOM TO MAKE BASIC DECISIONS
7. WHICH GIVE CERTAIN FRANCHISEES PREFERENTIAL TREATMENT
8. WHOSE REAL BUSINESS IS ONLY IN SELLING FRANCHISES
9. WHO DECEPTIVELY MINIMIZE THE COST OF DOING BUSINESS
10. WHO ACCEPT AS FRANCHISEES PERSONS LACKING THE BASIC SKILLS,EDUCATION OR PERSONALITY TO EVER SUCCEED
11. WHO FAIL TO PROVIDE PROPER TRAINING AND CONTINUING SUPERVISION



MAJOR SOURCES OF FRANCHISE OPPORTUNITY INFORMATION

DAILY NEWSPAPERS

TRADE PUBLICATIONS

FRANCHISING PUBLICATIONS

FRANCHISOR EXHIBITIONS

FRANCHISE MARKETING AGENCIES

ORGANIZATIONS REPRESENTING THE FRANCHISE INDUSTRY

MAJOR SOURCES OF FRANCHISE OPPORTUNITY COUNSEL

CHAMBERS OF COMMERCE

COMMUNITY BUSINESS DEVELOPMENT COUNCILS

CREDIT BUREAUS

BETTER BUSINESS BUREAU

FRANCHISE MARKETING AGENCIES

BANKERS

LAWYERS

FRANCHISE INDUSTRY ASSOCIATIONS

Focal Points On

FRANCHISING

TOPIC EIGHTEEN

Management Development Program

SMALL BUSINESS ADMINISTRATION

What to look for in: A FRANCHISOR;

1. FINANCIAL STABILITY
2. PRODUCT SALEABILITY
3. SPECIFIC TERRITORY
4. FIRM AND EQUITABLE CONTRACT
5. CONTINUING ADEQUATE ASSISTANCE

SOME ADVANTAGES FRANCHISING CAN OFFER THE FRANCHISEE

1. OPPORTUNITY TO BEGIN A BUSINESS WITH LIMITED MANAGEMENT EXPERIENCE AND CAPITAL INVESTMENT, AND WITH BUILT-IN SAFEGUARDS
2. ASSISTANCE IN MAINTAINING A STANDARD QUALITY OF PERFORMANCE
3. BUSINESS TRAINING AND CONTINUED ASSISTANCE FROM EXPERIENCED MANAGEMENT
4. CHAIN BUYING POWER
5. PROVEN METHODS OF DOING BUSINESS
6. WELL DEVELOPED CONSUMER IMAGE AND GOODWILL AT START
7. COMPETENTLY DESIGNED FACILITIES, LAYOUT, DISPLAYS, FIXTURES
8. PROVEN AND WELL-KNOWN PRODUCTS AND SERVICES
9. RECORD KEEPING, ACCOUNTING AND INVENTORY CONTROL ASSISTANCE
10. NATIONAL PROMOTION AND PUBLICITY TIE-IN
11. STRENGTHENED FINANCIAL AND CREDIT STANDING
12. FAVORABLE INCOME POTENTIAL WITH LOW RISK OF FAILURE

SOME DISADVANTAGES OF FRANCHISING TO THE FRANCHISEE

CONSIDER THESE PROVISIONS:

1. FRANCHISE FEES-INITIAL AND CONTINUING
2. SHARING PROFITS WITH FRANCHISOR
3. SUBMISSION TO IMPOSED STANDARDIZED OPERATIONS
4. REQUIREMENT TO MAINTAIN ASSIGNED SALES GOALS
5. LACK OF FREEDOM TO INTRODUCE ADDITIONAL PRODUCTS TO FRANCHISOR'S MERCHANDISE OR SERVICE LINES
6. TIME REQUIRED IN PREPARING PERIODIC REPORTS FOR FRANCHISOR
7. CONTRACTS SLANTED TO THE ADVANTAGE OF THE FRANCHISOR, IN SOME FRANCHISE AGREEMENTS
8. RESTRICTED CONTROL IN MAKING MANAGEMENT DECISIONS

EVALUATING A FRANCHISE

The Franchisor

1. For how many years has the firm offering you a franchise been in operation?

2. Has it a reputation for honesty and fair dealing among those who currently hold a franchise?

3. Will the firm assist you with:

   (a) A management training program?
   (b) An employee training program?
   (c) A public relations program?
   (d) Capital?
   (e) Credit?
   (f) Merchandising ideas?

4. Will the firm assist you in finding a good location for your new business?

5. Is the franchising firm adequately financed so that it can carry out its stated plan of financial assistance and expansion?

6. Has the franchisor shown you any certified figures indicating exact net profits of one or more going firms which you have personally checked yourself?

7. Is the franchisor a one man company or a corporation with an experienced management trained in depth (so that there would always be an experienced man at its head)?

8. Exactly what can the franchisor do for you which you cannot do for yourself?

9. Has the franchisor investigated you carefully enough to assure itself that you can successfully operate one of their franchises at a profit both to them and to you?

The Franchise

10. Did your lawyer approve the franchise contract after he studied it paragraph by paragraph?

11. Does the franchise call upon you to take any steps which are, according to your lawyer, unwise or illegal in your state, county or city?

12. Does the franchise give you an exclusive territory for the length of the franchise or can the franchisor sell a second or third franchise in your territory?

13. Is the franchisor connected in any way with any other franchise company handling similar merchandise or services?

14. If the answer to the last question is "YES", what is your protection against this second franchisor organization?

15. Under what circumstances can you terminate the franchise contract and at what cost to you, if you decide for any reason at all that you wish to cancel it?

16. If you sell your franchise, will you be compensated for your goodwill or will the goodwill you have built into the business be lost by you?

YOU - the Franchisee

17. How much equity capital will you have to have to purchase the franchise and operate it until your income equals expenses? Where are you going to get it?

18. Are you prepared to give up some independence of action to secure the advantages offered by the franchise?

19. Do YOU really believe you have the inate ability, training, and experience to work smoothly and profitably with the franchisor, your employees, and your customers?

20. Are you ready to spend much or all of the remainder of your business life with this franchisor, offering his product or service to your public?

Your Market

21. Have you made any study to determine whether the product or service which you propose to sell under franchise has a market in your territory at the prices you will have to charge?

22. Will the population in the territory given you increase, remain static, or decrease over the next five years?

23. Will the product or service you are considering be in greater demand, about the same, or less in demand five years from now than today?

24. What competition exists in your territory already for the product or service you contemplate selling?

    (a) Non franchise firms?
    (b) Franchise firms?

This was prepared by Dr. Wilford L. White, Director, Small Business Guidance and Development Center, Howard University, Washington, D.C. 20001. Additional copies may be obtained, without cost by writing to Dr. White, or by duplicating this copy.

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency

Prospective Enterprises

Small Marketers Aids

No. 71

Washington, D. C.
First printed, September 1961
Revised August 1966

CHECKLIST FOR GOING INTO BUSINESS

By Staff Members of the Small Business Administration, Washington, D.C.

SUMMARY

People sometimes go into business for themselves without being fully aware of what is involved. Sometimes they're lucky and succeed. More often, they fail because they do not consider one or more of the ingredients needed for business success.

This checklist is designed to help you decide whether you are qualified or have considered the various phases of going into business for yourself. Careful thought now may help you to prevent mistakes and to avoid losing your savings and time later. Use this list as a starter. Consider each question as it applies to your situation. Check off each question only after you've made an effort to answer it honestly. Before you omit a question, satisfy yourself that it does not apply to your particular situation.

After each section, you will find a few references. If you have uncovered doubtful areas or weaknesses in your preparation, it is strongly recommended that you obtain these publications and study them. You will find it time well spent. Most of the references are available, free, on request from any SBA field office or the Small Business Administration, Washington, D.C. 20416. However, the notation "Supt. Docs." means that the item is for sale at the price indicated by the Superintendent of Documents, Washington, D.C. 20402 (not from SBA).

QUESTIONS TO CONSIDER

Are You the Type?

	Yes	No
1. Have you rated your personal traits such as leadership, organizing ability, perseverance, and physical energy?		
2. Have you had some friends rate you on them?		
3. Have you considered getting an associate whose strong points will compensate for your weak traits?		

REFERENCES: Starting and Managing a Small Business of Your Own (25¢ Supt. Docs.); SM 39, Balances Skills: Measure of Effective Managers, in *Marketers Aids Annual* 5 (45¢ Supt. Docs.); SM 46, Essential Personal Qualities for Small Store Managers; SM 114, Pleasing Your Boss The Customer.

What Are Your Chances for Success?

	Yes	No
4. Have you had any actual business experience?		
5. Do you have special technical skills, such as those needed by a plumber, electrician, mechanic, or radio repairman?		
6. Have you obtained some basic management experience working for someone else?		
7. Have you analyzed the recent trend of business conditions (good or bad)?		
8. Have you analyzed business conditions in the city and neighborhood where you want to locate?		
9. Have you analyzed conditions in the line of business you are planning?		
10. Have you determined what size business you plan to establish (dollar sales per year)?		
11. Have you built up a detailed set of figures on how much capital you will need to launch the business?		
12. Have you figured how much time you will need until the business income equals the expenses?		
13. Have you planned what net profit you believe you should make?		

Yes No

14. Will the net profit divided by the investment result in a rate of return which compares favorably with the rate you can obtain from other investment opportunities?

REFERENCES: Appraise Your Competitive Position to Improve Company Planning, in *Management Aids Annual No. 2* (55¢ Supt. Docs.); Appraising the Market for the Services You Offer, in *Marketers Aids Annual No. 2* (40¢ Supt. Docs.); Practical Business Use of Government Statistics (20¢ Supt. Docs.)

How Much Capital Will You Need?

15. Have you worked out what income from sales or services you can reasonably expect in the first 6 months? The first year? The second year?
16. Do you know what net profit you can expect on these volumes?
17. Have you made a conservative forecast of expenses including a regular salary for yourself?
18. Have you compared this income with what you could make working for someone else?
19. Are you willing to risk uncertain or irregular income for the next year? Two years?
20. Have you counted up how much actual money you have to invest in your business?
21. Do you have other assets which you could sell or on which you could borrow?
22. Have you some other source from which you could borrow money?
23. Have you talked to a banker?
24. Is he favorably impressed with your plan?
25. Do you have a financial reserve for unexpected needs?
26. Does your total capital, from all sources, cover your best estimates of the capital you will need?

REFERENCES: SM 102, Using Security to Get a Bank Loan; SM 107, Building Strong Relations With Your Bank; SM 110, Controlling Cash in Small Retail and Service Firms; A Handbook of Small Business Finance (35¢ Supt. Docs.)

Should You Share Ownership With Others?

27. Do you lack needed technical or management skills which can be most satisfactorily supplied by one or more partners?
28. Do you need the financial assistance of one or more partners?
29. Have you checked the features of each form or organization (individual proprietorship, partnership, corporation) to see which will best fit your situation?

REFERENCES: MA 80, Choosing the Legal Structure for Your Firm; MA 111, Steps in Incorporating a Business.

Where Should You Locate?

30. Do you know how much space you will need?
31. Do you know what type of building you will need?
32. Do you know of any special features you require in lighting, heating, ventilating, air conditioning, or parking facilities?
33. Have you listed the tools and equipment you need room for?
34. If the proposed location does not meet nearly all your requirements, is there a sound reason why you should not wait and continue seeking a more ideal location?
35. Have you checked the U.S. Census Bureau population figures?

REFERENCES: MRS 78, Site Evaluation for Small Retailers; Sizing Up Small Business Locations, in *Marketers Aids Annual No. 1* (45¢ Supt. Docs.); SBB 16, Store Location.

Should You Buy a Going Business?

36. Have you considered the advantages and disadvantages of buying a going business?
37. Have you compared what it would take to equip and stock a new business with the price asked for the business you are considering?
38. Have you learned why the present owner wants to sell?
39. Have you checked the owner's claims about the business with reports from an independent accountant's analysis of the figures?

	Yes	No
40. Have you checked with the company's suppliers to obtain their ideas of the value of the business?		
41. Do the suppliers think well of the proposition?		
42. Is the stock of merchandise a questionable buy? (Would a large proportion of it have to be disposed of at a loss? Is any of it out of date, unsalable, or not usable?)		
43. Are the physical facilities old or in poor condition and, hence, overvalued?		
44. Are you sure the accounts receivable are worth the asking price?		
45. Is the present company's good will fairly valued?		
46. Are you prepared to assume the liabilities, and are the creditors agreeable?		
47. Has your lawyer checked to see if the title is good and if there is any lien against the assets?		
48. Are there any back taxes to pay?		
49. Have the sales been temporarily increased by conditions which are not likely to continue?		

REFERENCES: Key Factors in Starting a New Plant, in _Management Aids Annual No. 5_ (45¢ Supt Docs.); SM 20, Buying a Small Going Concern.

Are You Qualified to Supervise Buying and Selling?

	Yes	No
50. Have you estimated your total stock requirements?		
51. Do you know in what quantities users buy your product or service?		
52. Do you know how often users buy your product or service?		
53. Have you made a sales analysis to determine major lines to be carried?		
54. Have you decided what characteristics you will require in your goods?		
55. Have you set up a model stock assortment to follow in your buying?		
56. Have you investigated whether it will be cheaper to buy large quantities infrequently or in small quantities frequently?		
57. Have you weighed price differentials for large orders against capital and space tied up?		
58. Have you decided what merchandise to buy direct from manufacturers?		
59. Will you make your account more valuable to your suppliers by concentrating your buying with a few of them?		
60. Have you worked out control plans to insure stocking the right quantities?		

REFERENCES: SM 97, Steps in Making a Business Decision; SM 100, Make Selling Attractive to Salespeople; SM 113, Quality and Taste as Sales Appeals; SM 116, How to Select a Resident Buying Office; SM 120, Building Good Customer Relations SBB 37, Buying for Retail Stores.

How Will You Price Your Products and Services?

	Yes	No
61. Have you determined what prices you will have to charge to cover your costs and obtain profit?		
62. Do these prices compare favorably with prices of competitors?		

REFERENCES: How to Price a New Product, in _Management Aids Annual No. 3_ (45¢ Supt. Docs.); SM 105, A Pricing Checklist for Managers; SM 21, Pricing and Profits in Small Stores.

What Selling Methods Will You Use?

	Yes	No
63. Have you studied the sales promotional methods used by competitors?		
64. Have you outlined your own sales promotion policy?		
65. Have you studied why customers buy your product (service, price, quality, distinctive styling, other)?		
66. Will you do outside selling?		
67. Will you advertise in the newspapers?		
68. Will you do direct mail advertising?		
69. Will you use posters and handbills?		
70. Will you use radio and television advertising?		

REFERENCES: SM 16, Improving Personal Selling in Small Business; SM 96, Checklist for Successful Retail Advertising; SM 109, Stimulating Impulse Buying for Increased Sales; SBB 20, Advertising-Retail Store.

How Will You Manage Personnel?

	Yes	No
71. Will you be able to hire satisfactory employees, locally, to supply skills you lack?		

Yes No

72. Do you know what skills are necessary?
73. Have you checked the prevailing wage scales?
74. Have you a clear-cut idea of what you plan to pay?
75. Have you considered hiring someone now employed by a competitor?
76. Have you checked on the pros and cons of doing so?
77. Have you planned your training procedures?

REFERENCES: SM 103, Revitalize Personal Selling in Your Store; Sales Training for Small Wholesalers, in Marketers Aids Annual No. 1 (45¢ Supt Docs.); SBB 23, Training Retail Sales People; Sales Training for the Smaller Manufacturer (25¢ Supt. Docs.)

What Records Will You Keep?

78. Have you a suitable bookkeeping system ready to operate?
79. Have you planned a merchandise control system?
80. Have you obtained standard operating ratios for your type of business to use as guides?
81. Have you provided for additional records as necessary?
82. Have you a system to use in keeping a check on costs?
83. Do you need any special forms?
84. Have you made adequate provision for having your record keeping done?

REFERENCES: MA 75, Protecting Your Records Against Disaster in Management Aids Annual No. 5 (45¢ Supt. Docs.); SM 94, Keeping Score With Effective Records; SBB 15, Record Keeping Systems--Small Store and Service Trade.

What Laws Will Affect You?

85. Have you investigated what, if any, licenses to do business are necessary?
86. Have you checked the health regulations?
87. Are your operations subject to interstate commerce regulations?
88. Have you seen your lawyer for advice on how to meet your legal responsibilities?

REFERENCES: SM 118, Legal Service for Small Retail and Service Firms; SM 42, FTC and Guides Against Deceptive Pricing in Marketers Aids Annual 4 (35¢ Supt. Doc.) SM 24, Small Business and the Federal Trade Commission, in Marketers Aids Annual 2 (40¢ Supt. Docs.)

What Other Problems Will You Face?

89. Have you worked out a system for handling your tax requirements?
90. Have you arranged for adequate insurance coverage?
91. Have you worked out a way of building a management team?
92. Does your family (if any) agree that your proposed venture is sound?
93. Do you have enough capital to carry accounts receivable?
94. Will you sell for credit?
95. Have you worked out a definite returned goods policy?
96. Have you considered other management policies which must be established?
97. Have you planned how you will organize and assign the work?
98. Have you make a work plan for yourself?

REFERENCES: MA 103 Organizing the Owner-Manager's Job; SM 101, Pointers for Developing Your Top Assistant; Building Sound Credit Policies for Small Stores, in Marketers Aids Annual 1 (45¢ Supt. Docs.); SM 49, Improving Collections from Credit Sales in Marketers Aids Annual 5 (45¢ Sup. Doc.); Business Insurance, in Management Aids Annual No. 1 (75¢ Supt. Docs.); How Good Records Aid Income Tax Reporting, in Management Aids Annual No. 3 (45¢ Supt. Docs.); Appeal Procedures for Income Tax Cases, in Management Aids Annual No. 4 (45¢ Supt. Docs.)

Will You Keep Up To Date?

99. Have you a plan for keeping up with new developments in your line of business?
100. Have you a small group of qualified advisors from whom you can get help in solving new problems?

REFERENCES: SM 99, Remodeling for Better Retailing; SM 108, Building Repeat Business; SM 112, Sales Potential and Market Shares.

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency
Prospective Enterprises

Small Marketers Aids
No. 115

Washington, D. C.
October 1965

ARE YOU READY FOR FRANCHISING?

By A. L. Tunick

President, Chicken Delight, Inc., Rock Island, Illinois
and
Charter President of the International Franchise Association

SUMMARY

Franchising can be used by investors who want to start a small retail or service business of their own or by existing small marketers who want to expand their activities. In either case, the risk is reduced because the reputation of the franchised product or service helps to insure sales and because the management assistance and advice which many franchisors provide contribute to profits.

The key to franchising is the franchise contract. The best way to evaluate one is to get answers to questions about investment requirements, franchise fees, cancellation clauses, and various restrictions.

Whether franchising should be used depends, to a great extent, on the individual situation. This Aid discusses the advantages and disadvantages of franchising as they apply to varying situations. It points out that success depends on careful selection of a franchise and offers suggestions which should be useful in finding the right one.

The business "revolution" called franchising has caught the imagination of many small marketers. There are good reasons for it.

For the small investor, franchising minimizes the risk of failure because he can start in business under the image of a corporate name and trade mark and because he receives training and management assistance from experienced personnel. Sometimes, he is also offered financial assistance, making it possible for him to get started in a business of his own with less than the usual amount of cash.

In addition, franchising makes it possible for the small investor to associate himself with a regional, national, and sometimes international organization. From the standpoint of companies offering franchises--the franchisors--this type of business operation makes possible rapid expansion.

Whether you are ready for franchising depends on several things. Your present situation is one. If you're thinking of closing out your present store and opening a franchise store, for example, your answer to the question might be different from what it would be if you intend to start a franchise operation. Your answer would be different, of course, if you were considering the possibility of adding a franchised line, or lines, to an existing business.

In addition, whether or not franchising is for you depends on the kind of contract you would have to sign. The consideration of how much of your independence you would have to give up is also important.

As in any other type of business undertaking, your return in franchising is related directly to the amount of time and money you invest. Contrary to what some people may think, franchising is not a get rich quick deal. Nor is it an easy road to expansion for the franchisor--the manufacturer or distributor. There are dangers in franchising, for both franchisor and franchisee.

However, you can largely avoid the pitfalls when you know what franchising is and understand its advantages and disadvantages. You should also know where and how to get the facts to evaluate the prospects and profit potential of a franchise opportunity.

WHAT IS FRANCHISING?

Franchising is essentially a system of distribution under which an individually owned business is operated as though it were part of a large chain, complete with trade marks, uniform symbols, design, equipment, and standardized services or products. Franchising can be used for almost any type of business.

As a marketing technique, franchising is uniquely American. It began before the turn of the century when automobile manufacturers and petroleum refiners licensed new car dealers and gasoline service stations to retail their products in assigned areas. These retailers were supported with nationwide advertising and publicity. From these beginnings, the idea was picked up for drugstores, variety drygoods, and auto parts stores. Soon added were such services as dance studios and in-the-home rug cleaning, to name two.

Franchising began to flourish after World War II because opportunities were offered to small investors to operate franchised roadside businesses--primarily drive-in food and ice cream stands. When such drive-ins began to spread all over the American landscape, franchising became a magic word.

Today, hundreds of companies market many products and services through franchised outlets. Moreover, some of the best-known and oldest names in American industry are using franchised stores to expand into new markets with new or established products and services.

THE FRANCHISE CONTRACT

The license, or franchise contract is the key to franchising success. In it are the ingredients of experience that assure success. The contract can also contain the seeds for disappointment and discontent which can spell failure for the investor as well as the parent company.

In effect, a franchise contract is an investment agreement between the franchisor--sometimes known as the parent company--and the franchisee who is the investor. Contracts may range from a simple one-page memorandum of agreement to highly complex documents in which every conceivable detail of business operation is spelled out.

In some instances, contracts, in addition to specifying the exact products and services which a franchisee may sell under the parent company's name, dictate the hours and days of business as well as the types of uniforms, if any, to be worn by franchisees and their employees.

You should bear in mind that there is no standard franchise agreement any more than there is a uniform code of business practice. Nor is there any special significance to a simple contract as compared with a complex one. A great deal depends on the type of business being franchised and the method the parent company uses for selecting franchisees.

In all cases, however, franchise contracts should never be signed without legal counsel. Nowadays, the most reputable franchising companies insist that prospective investors do not sign until they have consulted attorneys or at least close family advisors, friends, accountants, or their bankers.

Although practically no two franchise contracts are alike, certain essential elements should be checked, or questioned if they are not present in contracts. One of the best ways to evaluate a franchise contract is to seek the answers to the following questions:

- Is there a franchise fee? If so, what is the basis for it?
- Are there continuing royalties?
- What is the total cash investment required, and what are the terms for financing the balance?
- Does the cash investment include payment for fixtures and equipment?
- How do prices for fixtures and equipment compare with competitive prices in the open market?
- Will you be required to participate in company-sponsored promotion and publicity by contributing a percentage of profits to an "advertising fund?" If so, will you have the right to veto any increase in contributions to the "fund?"
- If the parent company's product or service is protected by patent or liability insurance, is the same protection extended to you?
- Under what conditions may your franchise be cancelled?
- What special form of continuing assistance does the parent company obligate itself to give you after you are operating the business?
- Under what terms may you sell the business to whomever you please at whatever price you may be able to obtain?
- Will you be compelled to sell any new products introduced by the parent company after you have opened the business?
- How can you terminate your agreement if you are not happy for some reason?
- In essence, does the course you want to take parallel that of the franchisor? Does his success depend upon your success?

ADVANTAGES AND DISADVANTAGES

Generally, the principal advantage of franchising is that it enables you, as an investor, to capitalize on experience that you might otherwise have to obtain the hard way--through trial and error. The parent company uses its experience in business locations, management, advertising, publicity, product research and development, and so on to enable its franchisees to start and operate their outlets with optimum efficiency, maximum profitability, and minimum friction.

When the company's products are proven and well-known products, your store has an "instant" pulling power. On your own, it probably would take years of promotion and considerable investment to build such an identity and goodwill.

The principal disadvantage of franchising is the subjugation of your personal identity to that of the parent company, which has tremendous sums of money invested in building and maintaining its identity for your use. If you enjoy having your business known by your name, a franchise store may not be for you. On the other hand, the increased sales and profits which you might make with a franchise arrangement could outweigh the satisfaction of operating under your name. You have to decide, of course.

Deeper than the loss of personal identity is the fact that in a franchise operation you cannot make all the rules. Contrary to the many "be your own boss" lures in franchise advertisements, you may not truly be your own boss. The extent to which you can manage depends on the franchise contract.

You may have no effective voice in deciding your own future or the products you want to sell. And, as was mentioned earlier in this Aid, your hours and days of business may be specified in the contract. You have to live by the rules of your franchise contract so be sure that they are acceptable to you before you sign it.

Perhaps a brief look at the parent company's side will be helpful in understanding some of the rules that are in the contract. A manufacturer or distributor starts a franchising operation because he sees the opportunities to trade his proven experience and known product acceptance for your money and time. Thus he can increase his sales at a lower cost than if his company had to put up all the money.

A big problem for the franchisor is that of picking the right kind of people to run his franchised outlets. The parent company has the disadvantage of having to deal with individuals who, when they become successful, may forget about the parent company's "helping hand" that boosted them to prosperity. "They've got nothing to offer me," is the way some of these retailers feel in this stage. They think that they could have been successful without the parent company.

Even when the right kind of people are picked, the franchisor has serious problems in administration and control. After all, the franchisees are individual small businessmen--not company-employed managers. Therefore, a reputable parent company tries to use a contract which contains rules with which it and the outlet operator can live in a team framework, if not in a team spirit.

HOW FRANCHISEES ARE CHOSEN

When you seek a franchise which you feel is right for you, you may be disappointed if you aren't aware of how manufacturers and distributors choose their franchisees. They get prospects in a variety of ways. Most advertise for them in the "business opportunities" sections of newspapers and magazines. Some rely entirely on the word-of-mouth recommendations of their existing franchisees, and others recruit franchisees through exhibits at trade shows and business conventions.

Many techniques and variables exist in choosing from franchisee prospects. Some parent companies, for instance, will select no franchisees who does not agree to accept a minimum period of training. Others require psychological or aptitude tests. Still others rely entirely on comprehensive questionnaires and personal interviews.

Sometimes, the process begins with a parent-company representative interviewing the prospective franchisee in his home. This interview is followed by a final interview at the parent-company's headquarters. If you refuse to travel to headquarters for this interview, many franchisors will disqualify you immediately. They feel that such refusal indicates a lack of real interest in the opportunity they offer.

FINDING THE RIGHT FRANCHISE

In looking for a franchise that is right for you, you should watch out for the "fast buck" operators. The rapid growth of franchising has attracted an unsavory group of these operators who will take you if they can.

They are sometimes called "front money men." Essentially, they offer nothing more than the sale of equipment and a catchy business name. Once they sell you the equipment, they do not care whether you succeed or fail.

Thus, it is important when choosing a franchise to be certain that you are dealing with a reputable company. You should check with the local Better Business Bureau, the National Better Business Bureau, the local Chamber of Commerce, and local bankers. In checking, you can often obtain information by telephone that would not be put in letter form. An almost indispensable "research tool" is a full credit report on the company offering the franchise and its principals.

One of the best techniques for checking is to ask the company to provide you with a list of its existing franchisees in the area which you are considering. From this list, you should select several names and visit their stores during business hours.

By spending at least one full day at each location you can get an idea of what's going on. How many customers come in? What do they buy? What amount? And so on. You should also take time to ask the franchisees about the business. Most good parent companies encourage their franchisees to answer all questions for prospective investors.

When checking on a parent company, some important questions to ask are:

- When was the business established?
- Will its owners give you a specimen contract to study with the advice of legal counsel?

- Is there something with respect to the franchise or its operation which would make the franchisee ineligible for special financial assistance or other benefits accorded by Federal, State, or local governments to small business concerns?
- How does the company provide continuing assistance for its franchisees? Are there supervisors who visit regularly? Or only when called to help solve problems?
- How does the company resolve its differences with franchisees?
- How many franchisees are now operating?
- What has been the "mortality" or failure rate among franchisees?

LIST YOUR REQUIREMENTS

You should keep in mind that the most successful franchisee is one who chooses a business on the basis of understanding his own needs and requirements. Some people either overlook, or are not aware of the fact that franchising requires as much hard work as any other retail business. The parent company teaches the franchisee, but nobody will do the work for him.

To choose wisely in franchising, you should list your requirements for success by asking yourself the following questions:

- Why do I want a franchised business rather than one I'd have to start entirely on my own?
- Am I capable of accepting supervision, even though I will presumably be my own boss?
- Am I prepared to accept rules and regulations with which I may not agree?
- Will I be content with owning only one business location where I may not be able to expand as I desire?
- Can I afford the period of training involved?

And the person who has never been in business for himself, should ask whether he has enough confidence to be a self-starter after his training and close supervision is over. After all, the unknown quantity in franchising is the person who seeks a franchise. Has he made an honest evaluation of his desires, his abilities, and his willingness to work within a cooperative framework?

FOR FURTHER INFORMATION

Businessmen interested in the subject of franchising may wish to consult the following references. This list is necessarily brief and selective. However, no slight is intended toward authors whose works are not mentioned.

The Franchise Annual, 1965. $2. National Franchise Reports, 333 North Michigan Avenue, Chicago, Ill. 60601.

The Franchise System of Distribution. (A research report sponsored by the Small Business Administration). 1963. $2.50. Research Division, School of Business Administration, University of Minnesota, Minneapolis, Minn. 55455.

"The Franchise System of Distribution," *Management Research Summary* No. 172. Free. Small Business Administration, Washington, D.C. 20416.

The Franchise Boom: How You Can Profit in It, by Harry Kursh. 1962. $7.95. Prentice-Hall, Inc., Englewood Cliffs, N.J. 07631.

Modern Franchising Magazine. $2 per year. Modern Franchising Magazine, Inc., 1085 Walnut Street, Des Plaines, Ill. 60016.

The Monthly Report. $12 per year. National Franchise Reports, 333 North Michigan Ave., Chicago, Ill. 60601.

"A 'Mom & Pop' Business of Your Own," *Changing Times.* March 1965. $6 per year. The Kiplinger Washington Editors, Inc., Editors Park, Md. 20782.

Franchise Company Data. Task Force for Equal Opportunity in Business. October 1965. Free. U.S. Department of Commerce, Washington, D.C. 20230.

Still another source of information is the International Franchise Association, Inc., 333 North Michigan Ave., Chicago, Ill. 60601.

Reprinted 1966

SMALL BUSINESS
ADMINISTRATION
U. S. Government Agency

Management
Research Summary

THE FRANCHISE SYSTEM OF DISTRIBUTION

By *E. H. Lewis*, Professor of Marketing, and *R. S. Hancock*, Professor of Marketing
School of Business Administration, University of Minnesota, Minneapolis, Minnesota

HIGHLIGHTS

In general, the purchaser of a franchise can expect to be obligated to (1) a minimum investment of money, (2) a standardized inventory and/or equipment package; (3) the standard quality level, operating procedures, and promotional efforts of the system; and (4) the royalty or franchise fees.

Franchisees may be permitted by the franchise agreement to operate more than one unit of the same company; but almost all franchisors specify that no competing lines may be carried and no business of a competing nature conducted. Also, the franchise agreement often restricts franchisees from establishing a competing business in the franchise area for from 2 to 5 years after the franchise is terminated.

Franchisees operating a seasonal business are usually required to be open a minimum number of hours per day and days per year.

When a market supplier distributes his goods or services through franchises, he grants distribution rights to a limited number of firms. A franchise may be granted for one product or service, for a line of products, or for an entire business enterprise. The study reported in this Summary is concerned primarily with the latter. Its findings are based on the experiences of a sample of both franchisors and franchisees.

FRANCHISOR POLICIES

The purchaser of a franchise (the franchisee) is an independent businessman, but his association with a franchise group or system involves responsibilities as well as rights. Just what these responsibilities will be depends on the type of business and the complexity of its operation.

In general, a franchisee can expect to be obligated to (1) a minimum investment of money; (2) a standardized inventory and/or equipment package; (3) the standard quality level, operating procedures, and promotional efforts of the system; and (4) the royalty or franchise fees.

• Selecting Franchisees

Selecting a franchisee usually involves a written application, reference checks, a credit investigation, and at least one interview. Most franchisors do not require that the franchisee have any specified amount of formal education. They are more concerned with his business background, interest, and willingness to work hard.

Some franchisors accept part-time franchisees, but most of them want full-time people. Franchisees, however, may be

---

AVAILABILITY OF THE FULL REPORT

Copies of the full report, entitled "The Franchise System of Distribution," may be purchased for $2.50 from Research Division, School of Business Administration, University of Minnesota, Minneapolis, Minnesota, 55455. Make checks payable to the University of Minnesota.

This report was prepared under the Small Business Management Research Grant Program of SBA. It may be reviewed at any SBA field office or at certain libraries whose addresses may be obtained from the SBA field offices or from the Small Business Administration, Washington, D.C. 20416. The report was published in 1963.

permitted to operate additional units after the first unit is well established.

• Capital Requirements and Other Financial Aspects of the Franchise

Requirements for initial capital vary from $1,000 or less to $100,000 or more, depending largely on the type of business. Variations within a franchise organization depend on the scale of operations the franchisee wishes to establish.

Payment for the franchise is made in various ways. The franchisor may charge an initial fee, or he may require royalty payments based on the franchisee's sales or purchases of operating materials.

The franchise fee is frequently a flexible amount written into the contract to meet the particular situation. In an area of high potential, the fee may be higher than in an area of lower potential. Or the first franchisees enrolled in a new venture may pay a lower fee than those accepted after the system is established.

Other sources of income for the franchisor include profit on materials and supplies sold to the franchisee, charges for special services (accounting and tax services, for example), and assessments such as payments toward a national advertising program. Equipment is sometimes sold, but more often it is leased. Typically, the franchisor draws his income from some combination of these sources.

Some franchisors give the franchisee the choice of paying a lump sum at the start or making payments over a specified period of time. Others require a down payment and either finance the balance themselves or guarantee a bank loan with the dealer's inventory as security. For purchases by franchisees, some franchisors give rather liberal credit terms, but many extend no credit at all.

• Area Protection of Franchisee

Some franchisors have definite policies for area protection of their franchisees. Others do not. The better franchises give protection for segments of cities, entire cities, or metropolitan areas. Franchisees receive all inquiries from their areas and get credit for all sales made in them.

Once an area or a location has been assigned to a franchisee, the franchisor wants to have a going establishment as quickly as possible. Consequently, the contract often specifies that a franchisee must start building or be in business within a given period of time.

• Liability for Third Party Claims

Franchisors are usually concerned about the possibility of being held responsible for claims arising from actions of franchisees. Therefore, franchise contracts often stress the point that the franchisee is an independent contractor and not the agent or employee of the franchisor. The franchisor may also require the franchisee to carry liability insurance covering both personal and property damage.

• Location and Physical Appearance

Some franchisors retain the right to pass judgment on both the location and the building in which the franchisee proposes to do business. Others may secure an option on a site and make it available to an interested franchisee. Or the facilities may be owned by the franchisor and leased to the franchisee.

The appearance of individual establishments is an important tie-in among the units of many franchise systems. Customers expect to recognize a unit of the system instantly and to find in all units the same standards of lighting, cleanliness, decor, and so on. As a result, some franchisors furnish building and layout specifications that must be followed in detail. After the business is operating, a satisfactory level of maintenance is required.

• Control Over Purchases and Lines Carried

Where special formulas are involved, the materials must be purchased from the franchisor. In other cases, special discounts may be offered.

Franchisors generally require that certain specified items, at least, be purchased from them or from designated suppliers. They may also restrict to some degree the types of items the franchisee is permitted to sell. Almost all specify that no competing lines may be carried and no business of a competing nature conducted.

• Performance Controls

Some franchisors set up sales goals that the franchisee is expected or required to attain. Franchisees operating a seasonal business are usually required to be open a minimum number of hours per day and days per year. Franchisors in many fields also establish quality and service standards.

- Pricing

The most common policy of franchisors regarding the pricing of their goods and services by franchisees is to issue a suggested price list and let the franchisee set prices in terms of his own competitive situation. Some franchisors establish the maximum price the franchisee may charge, and some specify the exact prices at which the franchised products must be sold.

- Promotional Activities

Advertising campaigns using national media have been developed by several franchisors in support of their franchisees. At times, the franchisor may also wish to do some local advertising, especially when a new establishment is being opened.

Another advertising service of major importance to franchisees is the central preparation of newspaper mats, direct-mail material, radio/TV tapes, films, point-of-sale display material and signs, highway signs, handbills, leaflets, house organs, advertising novelties, and so on. These are usually sold to franchisees.

The franchisee is expected to engage in local promotion and sometimes to contribute to the national advertising program.

- Recordkeeping

In order to control and standardize some of the key operating features of a franchise system, the franchisor may develop record forms which the franchisee must use. He may, for instance, require periodic operating statements on a standardized form.

Many franchisors develop accounting and inventory-control systems and prepare tax materials for their dealers. Some issue excellent accounting manuals.

- Training Programs

Training programs for new franchisees range from a few days' help from a supervisor to training at centralized facilities. Frequently, new franchisees are trained on the premises of established dealers. Refresher training sessions are also beginning to appear in the franchise field.

Traveling supervisors spend a large part of their time working with new franchisees. They also advise established firms, and most franchisors are prepared to send someone, an expert, whenever a franchisee needs help with a pressing problem.

Quite a number of franchisors have developed comprehensive management manuals. In addition, they send out regular mailings of house organs, bulletins, newsletters, and leaflets covering various aspects of their operations.

- Termination of the Franchise

Franchise rights are given for a period of several years and are usually renewable. In some cases, the term of the agreement is 20 years or more.

Causes for which the franchise may be terminated are often specified in the contract. Typical reasons are: (1) failure to attain a satisfactory level of business; (2) failure to operate regularly or for the specified minimum period; (3) failure to put enough time and effort into the business; (4) failure to maintain quality and service standards; (5) misuse of the franchisor's name, materials, or equipment; (6) attempts to transfer the franchise in violation of the contract; and (7) failure to cooperate with the franchisor.

Franchisees are most likely to terminate a franchise (1) for personal reasons, (2) because the franchise has not brought the income they expected, or (3) because the franchisor has not delivered what he promised.

Often the franchisor specifies that the business may not be transferred without his consent. Another frequent restriction is the prohibition against establishing a competing business. The time period during which this prohibition remains in effect typically ranges from 2 to 5 years. The protected area may extend as far as 50 miles from the franchise area.

PROBLEMS AND CRITICISMS

A problem of concern to both franchisors and franchisees is the legal status of this method of distribution. This question has been raised in the courts because franchise agreements have sometimes been used to restrain trade. The franchising industry, through the International Franchise Association, is well aware of this problem and has developed educational programs designed to prevent abusive and illegal practices.

Another major problem confronting franchisors is the difficulty of administering the many units within a franchise system as an organized whole rather than as so many separate organizations.

The most common specific problem reported by both franchisors and franchisees interviewed for the study was undercapitalization during the early stages of their operations. The respondents believed this pitfall could be avoided by improved planning, adequate provision for unforeseen contingencies, and better knowledge of outside sources of capital.

Some franchisees believed that selection methods used by franchisors needed improvement. Poor selection procedures were seen as weakening the system, to the detriment of all the dealers.

Most franchisees recognized the advantages of operating a franchised business, but a minority disliked some specific operating practices. Following are some of the criticisms expressed:

1. Franchisor fees, prices for supplies, and other charges are too high.
2. Operating and financial guides prepared by the franchisors are not realistic.
3. The franchisors' field men, merchandising experts, and others who visit the dealer do not show an awareness of local conditions.

CHOOSING A FRANCHISE

The majority of the franchisees interviewed had spent considerable time in finding their opportunity. The report states that a prospective investor should weigh his qualifications against the franchise opportunity and suggests the following questions to show the directions his inquiry should take.

1. What are your own special qualifications?
2. Have you enough capital to buy the franchise under consideration?
3. What is the reputation of the franchise company and its principals?
4. What are the terms of the contract? What are your rights and obligations under the franchise agreement?
5. What is the purpose of the franchise fee?
6. Is there a promising market for the product or service?

The full report lists several sources of information about franchises, including two periodicals dealing exclusively with franchising and franchise opportunities: National Franchise Reports and Modern Franchising.

ABOUT THE STUDY

The report is based on interviews with (1) 40 franchisees in the Minneapolis-St. Paul area, and (2) 40 franchisors located throughout the United States and representing a wide variety of commodity lines and services. Descriptive literature received from the franchisors was also used in constructing the material on franchisor policies and operating methods. Many quotations from actual contracts are used in the full report to illustrate the points discussed.

MRS-172:9-63

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency

MANAGEMENT AIDS **No. 170**
for small manufacturers

Washington, D. C. First printed February 1965 Revised May 1967

THE ABC'S OF BORROWING

Revised by members of The Staff, Financial Assistance,
Small Business Administration, Washington, D.C.

SUMMARY

Some small businessmen cannot understand why a lending institution refuses to lend them money. Others have no trouble getting funds, but they are surprised to find strings attached to their loans. Such owner-managers fail to realize that banks and other lenders have to operate by certain principles just as do other types of business.

This Aid discusses the following fundamentals of borrowing: (1) credit worthiness, (2) kinds of loans, (3) amount of money needed, (4) collateral, (5) loan restrictions and limitations, (6) the loan application, and (7) standards which the lender uses to evaluate the application. The SBA form is used to illustrate suggestions for filling out a loan application.

Inexperience with borrowing procedures often creates resentment and bitterness. The stories of three small businessmen illustrate this point.

"I'll never trade here again," Bill Smith* said when his bank refused to grant him a loan. "I'd like to let you have it, Bill," the banker said, "but your firm isn't earning enough to meet your current obligations." Mr. Smith was unaware of a vital financial fact, namely, that lending institutions have to be certain that the borrower's business can repay the loan.

Tom Jones lost his temper when the bank refused him a loan because he did not know what kind or how much money he needed. "We hesitate to lend," the banker said, "to businessmen with such vague ideas of what and how much they need."

John Williams' case was somewhat different. He didn't explode until after he got the loan. When the papers were ready to sign, he realized that the loan agreement put certain limitations on his business activities. "You can't dictate to me," he said and walked out of the bank. What he didn't realize was that the limitations were for his good as well as for the bank's protection.

Knowledge of the financial facts of business life could have saved all three men the embarrassment of losing their tempers. Even more important, such information would have helped them to borrow money at a time when their businesses needed it badly.

This Aid is designed to give the highlights of what is involved in sound business borrowing. It should be helpful to those who have little or no experience with borrowing. More experienced businessmen should find it useful in re-evaluating their borrowing operations.

IS YOUR FIRM CREDIT WORTHY?

The ability to obtain money when you need it is as necessary to the operation of your business as is a good location or the right equipment, reliable sources of supplies and materials, or an adequate labor force. Before a bank or any other lending agency will lend you money, the loaning officer must feel satisfied with the answers to the five following questions:

1. What sort of person are you, the prospective borrower? By all odds, the character of the borrower comes first. Next is his ability to manage his business.
2. What are you going to do with the money? The answer to this question will determine the type of loan--short- or long-term. Money to be used for the purchase of seasonal inventory will require quicker repayment than money used to buy fixed assets.
3. When and how do you plan to pay it back? Your banker's judgement as to your business ability and the type of loan will be a deciding factor in the answer to this question.

---

*All names in Aids are disguised.

4. Is the cushion in the loan large enough? In other words, does the amount requested make suitable allowance for unexpected developments? The banker decides this question on the basis of your financial statement which sets forth the condition of your business and/or on the collateral pledge.

5. What is the outlook for business in general and for your business particularly?

- Adequate Financial Data Is a "Must."

The banker wants to make loans to businesses which are solvent, profitable, and growing. The two basic financial statements he uses to determine those conditions are the balance sheet and profit-and-loss statement. The former is the major yardstick for solvency and the latter for profits. A continuous series of these two statements over a period of time is the principal device for measuring financial stability and growth potential.

In interviewing loan applicants and in studying their records, the banker is especially interested in the following facts and figures.

General Information: Are the books and records up-to-date and in good condition? What is the condition of accounts payable? Of notes payable? What are the salaries of the owner-manager and other company officers? Are all taxes being paid currently? What is the order backlog? What is the number of employees? What is the insurance coverage?

Accounts Receivable: Are there indications that some of the accounts receivable have already been pledged to another creditor? What is the accounts receivable turnover? Is the accounts receivable total weakened because many customers are far behind in their payments? Has a large enough reserve been set up to cover doubtful accounts? How much do the largest accounts owe and what percentage of your total accounts does this amount represent?

Inventories: Is merchandise in good shape or will it have to be marked down? How much raw material is on hand? How much work is in process? How much of the inventory is finished goods?

Is there any obsolete inventory? Has an excessive amount of inventory been consigned to customers? Is inventory turnover in line with the turnover for other businesses in the same industry? Or is money being tied up too long in inventory?

Fixed Assets: What is the type, age, and condition of the equipment? What are the depreciation policies? What are the details of mortgages or conditional sales contracts? What are the future acquisition plans?

WHAT KIND OF MONEY?

When you set out to borrow money for your firm, it is important to know the kind of money you need from a bank or other lending institution. There are three kinds of money: short-term money, term money, and equity capital.

Keep in mind that the purpose for which the funds are to be used is an important factor in deciding the kind of money needed. But even so, deciding what kind of money to use is not always easy. It is sometimes complicated by the fact that you may be using some of various kinds of money at the same time and for identical purposes.

Keep in mind that a very important distinction between the types of money is the source of repayment. Generally, short-term loans are repaid from the liquidation of current assets which they have financed. Long-term loans are usually repaid from earnings.

- Short-Term Bank Loans

You can use short-term bank loans for purposes such as financing accounts receivable for, say, 30 to 60 days. Or you can use them for purposes that take longer to pay off--such as for building a seasonal inventory over a period of 5 to 6 months. Usually, lenders expect short-term loans to be repaid after their purposes have been served: for example, accounts receivable loans, when the outstanding accounts have been paid by the borrower's customers, and inventory loans, when the inventory has been converted into saleable merchandise.

Banks grant such money either on your general credit reputation with an unsecured loan or on a secured loan--against collateral.

The unsecured loan is the most frequently used form of bank credit for short-term purposes. You do not have to put up collateral because the bank relies on your credit reputation.

The secured loan involves a pledge of some or all of your assets. The bank requires security as a protection for its depositors against the risks that are involved even in business situations where the chances of success are good.

- Term Borrowing

Term borrowing provides money you plan to pay back over a fairly long time. Some people break it down into two forms: (1) intermediate--loans longer than 1 year but less than 5 years, and (2) long-term--loans for more than 5 years.

However, for your purpose of matching the kind of money to the needs of your company, think of term borrowing as a kind of money which you probably will pay back in periodic installments from earnings.

- Equity Capital

Some people confuse term borrowing and equity (or investment) capital. Yet there is a big difference. You don't have to repay equity money. It is money you get by selling a part interest in your business.

You take people into your company who are willing to risk their money in it. They are interested in potential income rather than in an immediate return on their investment.

HOW MUCH MONEY?

The amount of money you need to borrow depends on the purpose for which you need funds. Figuring the amount of money required for business construction, conversion, or expansion--term loans or equity capital--is relatively easy. Equipment manufacturers, architects, and builders will readily supply you with cost estimates. On the other hand, the amount of working capital you need depends upon the type of business you're in. While rule-of-thumb ratios may be helpful as a starting point, a detailed projection of sources and uses of funds over some future period of time--usually for 12 months--is a better approach. In this way, the characteristics of the particular situation can be taken into account. Such a projection is developed through the combination of a predicted budget and a cash forecast.

The budget is based on recent operating experience plus your best judgment of performance during the coming period. The cash forecast is your estimates of cash receipts and disbursements during the budget period. Thus, the budget and the cash forecast together represent your plan for meeting your working capital requirements.

To plan your working capital requirements, it is important to know the "cash flow" which your business will generate. This involves simply a consideration of all elements of cash receipts and disbursements at the time they occur. These elements are listed in the profit-and-loss statement which has been adapted to show cash flow in the box on this page. They should be projected for each month. Note that it shows "Bank Loans To Be Obtained" as well as "Bank Loans To Be Repaid."

P&L STATEMENT ADAPTED TO SHOW CASH FLOW

The profit and loss statement elements listed below have been adapted to show cash flow. Note that it shows "Bank Loans To Be Obtained" as well as "Bank Loans To Be Repaid." The P and L statement should be projected for each month of the year.

Monthly Operations	
Net sales	$ ______
Less: Material used	______
Direct labor	______
Other mfging expense	______
Cost of goods sold	$ ______
Gross profit	$ ______
Less: Sales expense	______
General and administrative expense	______
Operating profit	$ ______
Cash Flow	
Cash balance (beginning)	$ ______
Receipts from receivables	______
Total available cash	$ ______
Less Disbursements	
Trade payables	______
Direct labor	______
Other mfging expense	______
Sales expense	______
General and administrative expense	______
Fixed asset additions	______
Bank loans to be repaid	______
Total disbursements	$ ______
Indicated cash shortage	$ ______
Bank loans to be obtained	$ ______
Cash balance (ending)	$ ______
Materials purchased	$ ______
Month-end position	
Accounts receivable	$ ______
Inventory	$ ______
Accounts payable	$ ______
Bank loans payable	$ ______

WHAT KIND OF COLLATERAL?

Sometimes, your signature is the only security the bank needs when making a loan. At other times, the bank requires additional assurance that the money will be repaid. The kind and amount of security depends on the bank and on the borrower's situation.

If the loan required cannot be justified by the borrower's financial statements alone, a pledge of security may bridge the gap. The types of security are: endorsers, comakers, and guarantors; assignment of leases;

trust receipts and floor planning; chattel mortgages; real estate; accounts receivables; savings accounts; life insurance policies; and stocks and bonds. In a substantial number of States where the Uniform Commercial Code has been enacted, paperwork for recording loan transactions will be greatly simplified.

• Endorsers, Co-makers, and Guarantors

Borrowers often get other people to sign a note in order to bolster their own credit. These endorsers are contingently liable for the note they sign. If the borrower fails to pay up, the bank expects the endorser to make the note good. Sometimes, the endorser may be asked to pledge assets or securities that he owns.

A co-maker is one who creates an obligation jointly with the borrower. In such cases, the bank can collect directly from either the maker or the co-maker.

A guarantor is one who guarantees the payment of a note by signing a guaranty commitment. Both private and government lenders often require guarantees from officers of corporations in order to assure continuity of effective management. Sometimes, a manufacturer will act as guarantor for one of his customers.

• Assignment of Leases

The assigned lease as security is similar to the guarantee. It is used, for example, in some franchise situations.

The bank lends the money on a building and takes a mortgage. Then the lease, which the dealer and the parent franchise company work out, is assigned so that the bank automatically receives the rent payments. In this manner, the bank is guaranteed repayment of the loan.

• Warehouse Receipts

Banks also take commodities as security by lending money on a warehouse receipt. Such a receipt is usually delivered directly to the bank and shows that the merchandise used as security either has been placed in a public warehouse or has been left on your premises under the control of one of your employees who is bonded (as in field warehousing). Such loans are generally made on staple or standard merchandise which can be readily marketed. The typical warehouse receipt loan is for a percentage of the estimated value of the goods used as security.

• Trust Receipts and Floor Planning

Merchandise, such as automobiles, appliances, and boats, has to be displayed to be sold. The only way many small marketers can afford such displays is by borrowing money. Such loans are often secured by a note and a trust receipt.

This trust receipt is the legal paper for floor planning. It is used for serial-numbered merchandise. When you sign one, you (1) acknowledge receipt of the merchandise, (2) agree to keep the merchandise in trust for the bank, and (3) promise to pay the bank as you sell the goods.

• Chattel Mortgages

If you buy equipment such as a cash register or a delivery truck, you may want to get a chattel mortgage loan. You give the bank a lien on the equipment you are buying.

The bank also evaluates the present and future market value of the equipment being used to secure the loan. How rapidly will it depreciate? Does the borrower have the necessary fire, theft, property damage, and public liability insurance on the equipment? The banker has to be sure that the borrower protects the equipment.

• Real Estate

Real estate is another form of collateral for long-term loans. When taking a real estate mortgage, the bank finds out: (1) the location of the real estate, (2) its physical condition, (3) its foreclosure value, and (4) the amount of insurance carried on the property.

• Accounts Receivable

Many banks lend money on accounts receivable. In effect, you are counting on your customers to pay your note.

The bank may take accounts receivable on a notification or a nonnotification plan. Under the notification plan, the purchaser of the goods is informed by the bank that his account has been assigned to it and he is asked to pay the bank. Under the nonnotification plan, the borrower's customers continue to pay him the sums due on their accounts and he pays the bank.

• Savings Accounts

Sometimes, you might get a loan by assigning to the bank a savings account. In such cases, the bank gets an assignment from you and keeps your passbook. If you assign an account in another bank as collateral, the lending bank asks the other bank to mark its records to show that the account is held as collateral.

• Life Insurance

Another kind of collateral is life insurance. Banks will lend up to the cash value of a life insurance policy. You have to assign the policy to the bank.

If the policy is on the life of an executive of a small corporation, corporate resolutions must be made authorizing the assignment. Most insurance companies allow you to sign the policy back to the original beneficiary when the assignment to the bank ends.

Some people like to use life insurance as collateral rather than borrow directly from insurance companies. One reason is that a bank loan is often more convenient to obtain and usually may be obtained at a lower interest rate.

SITUATIONS WHICH MAKE A BUSINESS INELIGIBLE FOR A SBA LOAN

The Small Business Administration cannot lend money in the following situations:

- If the company can get money on reasonable terms:
  - (1) From a financial institution
  - (2) By selling assets which it does not need in order to grow.
  - (3) By the owner's using, without undue personal hardship, his personal credit or resources of his partners or principal stockholders.
  - (4) By selling a portion of ownership in the company through a public offering or a private placing of its securities.
  - (5) From other Government agencies which provide credit specifically for the applicant's type of business or for the purpose of the required financing.
  - (6) From other known sources of credit.

- If the direct or indirect purpose or result of granting a loan would be to:
  - (1) Pay off a creditor or creditors of the applicant who are inadequately secured and in a position to sustain a loss.
  - (2) Provide funds for distribution or payment to the owner, partners, or shareholders.
  - (3) Replenish working capital funds previously used to pay the owner, partners, or shareholders.

- If the applicant's purpose in applying for a loan is to effect a change in ownership of the business; however, under certain circumstances, loans may be authorized for this purpose, if the result would be to aid in the sound development of a small business or to keep it in operation.

- If the loan would provide or free funds for speculation in any kind of property, real or personal, tangible or intangible.

- If the applicant is a charitable organization, social agency, society, or other nonprofit enterprise; however, a loan may be considered for a cooperative if it carries on a business activity and the purpose of the activity is to obtain financial benefit for its members in the operation of their otherwise eligible small business concerns.

- If the purpose of the loan is to finance the construction, acquisition, conversion, or operation of recreational or amusement facilities, unless the facilities contribute to the health or general well-being of the public.

- If the applicant is a newspaper, magazine, radio broadcasting or television broadcasting company, or similar enterprise.

- If any substantial portion (50 percent or more) of the net sales of the applicant is derived from the sale of alcoholic beverages.

- If any of the gross income of the applicant (or of any of its principal owners) is derived from gambling activities.

- If the loan is to provide funds to an enterprise primarily engaged in the business of lending or investments or to provide funds to any otherwise eligible enterprise for the purpose of financing investments not related or essential to the enterprise.

- If the purpose of the loan is to finance the acquisition, construction, improvement, or operation of real property that is, or is to be, held primarily for sale or investment.

- If the effect of granting of the financial assistance will be to encourage monopoly or will be inconsistent with the accepted standards of the American system of free competitive enterprise.

- If the loan would be used to relocate a business for other than sound business purposes.

- Stocks and Bonds

If you use stocks and bonds as collateral, they must be marketable. As a protection against market declines and possible expenses of liquidation, banks usually lend no more than 75 percent of the market value of high grade stock. On Federal Government or municipal bonds, they may be willing to lend 90 percent or more of their market value.

The bank may ask the borrower for additional security or payment whenever the market value of the stocks or bonds drops below the bank's required margin.

WHAT ARE THE LENDER'S RULES?

Lending institutions are not just interested in loan repayments. They are also interested in borrowers with healthy profit-making businesses. Therefore, whether or not collateral is required for a loan, they set loan limitations and restrictions to protect themselves against unnecessary risk and at the same time against poor management practices by their borrowers. Often some owner-managers consider loan limitations a burden.

Yet others feel that such limitations also offer an opportunity for improving their management techniques.

Especially in making long-term loans, the borrower as well as the lender should be thinking of: (1) the net earning power of the borrowing company, (2) the capability of its management, (3) the long range prospects of the company, and (4) the long range prospects of the industry of which the company is a part. Such factors often mean that limitations increase as the duration of the loan increases.

WHAT KINDS OF LIMITATIONS?

The kinds of limitations, which an owner-manager finds set upon his company depends, to a great extent, on his company. If his company is a good risk, he should have only minimum limitations. A poor risk, of course, is different. Its limitations should be greater than those of a stronger company.

Look now for a few moments at the kinds of limitations and restrictions which the lender may set. Knowing what they are can help you see how they affect your operations.

The limitations which you will usually run into when you borrow money are:

(1) Repayment terms.
(2) Pledging or the use of security.
(3) Periodic reporting.

A loan agreement, as you may already know, is a tailor-made document covering, or referring to, all the terms and conditions of the loan. With it, the lender does two things: (1) protects his position as a creditor (he wants to keep that position in as well a protected state as it was on the date the loan was made) and (2) assures himself of repayment according to the terms.

The lender reasons that the borrower's business should generate enough funds to repay the loan while taking care of other needs. He considers that cash inflow should be great enough to do this without hurting the working capital of the borrower.

● Covenants--Negative and Positive

The actual restrictions in a loan agreement come under a section known as covenants. Negative covenants are things which the borrower may not do without prior approval from the lender. Some examples are: further additions to the borrower's total debt, non-pledge to others of the borrower's assets, and issuance of dividends in excess of the terms of the loan agreement.

On the other hand, positive covenants spell out things which the borrower must do. Some examples are: (1) maintenance of a minimum net working capital, (2) carrying of adequate insurance, (3) repaying the loan according to the terms of the agreement, and (4) supplying the lender with financial statements and reports.

Overall, however, loan agreements may be amended from time to time and exceptions made. Certain provisions may be waived from one year to the next with the consent of the lender.

● You Can Negotiate

Next time you go to borrow money, thresh out the lending terms before you sign. It is good practice no matter how badly you may need the money. Ask to see the papers in advance of the loan closing. Legitimate lenders are glad to cooperate.

Chances are that the lender may "give" some on the terms. Keep in mind also that, while you're mulling over the terms, you may want to get the advice of your associates and outside advisors. In short, try to get terms which you know you company can live with. Remember, however, that once the terms have been agreed upon and the loan is made (or authorized as in the case of SBA), you are bound by them.

THE LOAN APPLICATION

Now you have read about the various aspects of the lending process and are ready to apply for a loan. Banks and other private lending institutions, as well as the Small Business Administration, require a loan application on which you list certain information about your business.

For purposes of explaining a loan application, this Aid uses the Small Business Administration's application for a small loan (SBA Form 6B)--one for $25,000 or less. The SBA form is more detailed than most bank forms. The bank has the advantage of prior knowledge of the applicant and his activities. Since SBA does not have such knowledge, its form is more detailed. Moreover, the longer maturities of SBA loans ordinarily will necessitate more knowledge about the applicant.

Before you get to the point of filling out a loan application, you should have talked with an SBA representative, or perhaps your accountant or banker, to make sure that your business is eligible for an SBA loan. Because of public policy, SBA cannot make certain types of loans. Nor can it make loans under certain conditions. For example, if you can get a loan on reasonable terms from a bank, SBA cannot lend you money. The owner-manager is also not eligible for an SBA loan if he can get funds by selling assets which his company does not need in order to grow. (For other examples, see page 5.)

When the SBA representative gives you a loan application, you will notice that most of its sections ("Application for Loan"--SBA Form 6B) are self-explanatory. However, some applicants have trouble with certain sections because they do not know where to go to get the necessary information.

Section 3--"Collateral Offered" is an example. A company's books should show the net value of assets such as business real estate and business machinery and equipment. "Net" means what you paid for such assets less depreciation.

If an owner-manager's records do not contain detailed information on business collateral, such as real estate and machinery and equipment, he sometimes can get it from his Federal income tax returns. Reviewing the depreciation which he has taken for tax purposes on such collateral can be helpful in arriving at the value of these assets.

If you are a good manager, you should have your books balanced monthly. However, some businesses prepare balance sheets less regularly. In filling out Section 7--"Balance Sheet as of _________ , 19, Fiscal Year Ends _______" of the SBA loan application, remember that you must show the condition of your business within 60 days of the date on your loan application. It is best to get expert advice when working up such vital information. Your accountant or banker will be able to help you.

Again, if your records do not show the details necessary for working up profit and loss statements, your Federal income tax returns (Schedule C of Form 1040, if your business is a sole proprietorship or a partnership) may be useful in getting together facts for Section 8 of the SBA loan application. This Section asks for "Condensed Comparative Statements of Sales, Profits or Loss, etc." You fill in the blocks appropriate to your form of business organization--corporation, partnership, or proprietorship--and attach detailed profit-and-loss statements.

● Insurance

SBA also needs information about the kinds of insurance a company carries. The owner-manager gives these facts by listing various insurance policies. If you place all your insurance with one agent or broker, you can get this information from him.

● Personal Finances

SBA also must know something about the personal financial condition of the applicant. Among the types of information are: personal cash position; source of income including salary and personal investments; stocks, bonds, real estate, and other property owned in the applicant's own name; personal debts including installment credit payments, life insurance premiums, and so forth.

EVALUATING THE APPLICATION

Once you have supplied the necessary information, the next step in the borrowing process is the evaluation of your application. Whether the processing officer is in a bank or in SBA, he considers the same kinds of things when determining whether to grant or refuse the loan. The SBA loan processor looks for:

(1) The borrower's debt paying record to suppliers, banks, home mortgage holders, and other creditors.

(2) The ratio of the borrower's debt to his net worth.

(3) The past earnings of the company.

(4) The value and condition of the collateral which the borrower offers for security.

The SBA loan processor also looks for: (1) the borrower's management ability, (2) the borrower's character, and (3) the future prospects of the borrower's business.

FOR FURTHER INFORMATION

Readers who wish to explore further the subject of borrowing may be interested in the references indicated below. This list is necessarily brief and selective. However, no slight is intended toward authors whose works are not mentioned.

The following *Management Aids for Small Manufacturers* are available free from the Washington, D.C. and field offices of Small Business Administration:

"Is Your Cash Supply Adequate?"--MA174.

"Financial Audits: A Tool for Better Management"--MA176.

The following *Small Marketers Aids* are available free from the Washington, D.C. and field offices of Small Business Administration:

"Controlling Cash in Small Retail and Service Firms"--SMA 110.

"Using Security to Get a Bank Loan"--SMA 102.

"Steps In Making A Business Decision"--SMA 97.

"Keeping Score With Effective Records"--SMA 94.

The following *Small Business Management Series* booklets published by SBA can be bought from the Superintendent of Documents, Washington, D.C. 20402. The year of publication and price are listed after each title.

A Handbook of Small Business Finance. SBMS NO. 15. 7th Ed. March 1965. 35 cents.

Ratio Analysis for Small Business. SBMS No. 20. 1960. 25 cents.

Guides for Profit Planning. SBMS NO. 25. 1960. 25 cents.

Management Aids for Small Manufacturers: Annual No. 12. 1966. 35 cents. (See the following chapters: "Financial Facts which Lenders Require," "Bank Loan Limitations: Living Within Them", and "Financial Planning in Closely Held Businesses".

Management Aids for Small Manufacturers: Annual No. 11. 1965. 40 cents. (See the following chapters: "What Kind of Money Do You Need?" and "Getting Money for Long-Term Growth".)

SMALL BUSINESS ADMINISTRATION
U. S. Government Agency

MANAGEMENT AIDS **No. 182**
for small manufacturers

Washington, D.C. March 1966

EXPANDING SALES THROUGH FRANCHISING

By **Al Lapin, Jr.**

President, International Industries, Inc., North Hollywood, California

SUMMARY

Franchising offers small companies a way to accelerate their growth--to increase sales. In this method of distribution, the small manufacturer can obtain new outlets for his products by granting franchises to men who are also small businessmen.

Many franchisees invest their money because they want to work for themselves. Furthermore, they want to affiliate with a going concern which makes profitable products rather than taking the risk of starting from scratch by themselves. These franchise investors are usually looking for a package which they can buy for a certain amount.

Aspects of putting together such a package are discussed in this Aid. Among them are: providing guidance for franchisees, testing with a pilot operation, factors which determine the amount of money needed by the franchisee and franchisor, the franchise agreement, and selling the package. Training the franchisee is also discussed.

Franchising is a system of distribution by which you, as a small manufacturer, may be able to widen the market for your products. You do this by granting distribution rights or a particular distribution right to a limited number of selected businesses. In effect, it increases the number of your outlets (1) which are owned fully by investors other than yourself or your company or (2) which are owned in "partnership" arrangements between outside investors and your company.

Franchising offers several advantages to you as a small manufacturer. One is rapid expansion. This method of distribution offers you an immediate source of growth capital without diminishing the ownership of the company. As a franchisor, you are limited only by the standards you set for granting your franchises since investment capital is supplied by the franchisees in most cases.

Reduced management overhead is another advantage. In franchising, the franchisee or his representative is the manager of the outlet. Thus, you do not have to hire managers as you would if you started your own stores. A franchise places ownership and management at the point-of-sale and thereby reduces the parent company's general management overhead.

Another advantage of franchising is that it provides a built-in community acceptance of your product. Customers are more receptive to trying a product when they buy it from a local citizen.

Finally, franchising provides a strong success motivation. Franchisees need to operate efficiently and profitably to protect their cash investment.

Whether your company can enjoy these advantages depends on the type of product you make or the service you offer, as well as the market you are trying to reach, and the buying habits of your ultimate consumer. Following are one or more of the conditions that have been found necessary for a successful franchise:

(1) A product or service that is distinctive and has a readily identifiable trademark so that the ultimate consumer will put forth more effort than usual to purchase it.

(2) A product that requires installation, an inventory of parts at the local level, and dealer (franchisee) responsibility for maintenance.

(3) A new product or service which needs restriction of outlets as a basis for obtaining dealer cooperation.

(4) A sufficiently large investment by the franchisee in equipment and/or inventory in return for which there is a relatively adequate markup.

FRANCHISEES NEED GUIDANCE

When the small manufacturer sells a franchise package, his company has to live with it for years. Therefore, it is essential to build a franchise program which will wear well for you and the franchisee. A standard pattern of good service and a unified image with which customers can identify works advantageously for each franchisee and you.

This fact means the franchisee has to have a pattern to go by when he sells your product. Without guidance on merchandising and profit making even the best program would soon break down into a hodge-podge.

When you insist that your franchisees merchandise in the same way, customers learn to expect the same system of service and the same product whenever they go into one of your outlets. But even more important to the franchisee is the protection which your system of control should provide him. When you insist that each outlet run so as to attract customers, you are protecting the investments of all the members in your franchising program as well as your own.

A system of controls should also help the franchisee to operate at a profit. A system of recordkeeping, for example, helps to spot quickly areas of potential trouble for the franchisee.

In considering the kinds of controls or system you need, two questions can be useful. First, what is necessary to insure that the franchisees operate according to the plan for attracting customers? And, what services should you, as the franchisor, furnish to help the franchisee operate at a profit?

TESTING WITH A PILOT OPERATION

After you have worked out the system under which your franchisees will operate, the next step is testing it with a pilot operation. This pilot outlet must be located in a "typical" business area. The location for your pilot operation has to be as similar as possible to the kinds of sites your franchisees will be using later on.

Using an average location--one as similar as possible to the kinds of sites your franchisees will be using--should give you two things: (1) figures which you can use for future planning and (2) assistance in selling the package to franchisees. When your pilot operation is in an average location, it is fairly easy for your franchise prospects to relate it to their own town or area.

Your pilot operation must feature exactly what you intend to sell potential franchisees. A person buys a franchise because it is a tested package and because he can see the kind of store in which he plans to invest.

In operating the pilot outlet, accounting procedures and other systems should be maintained exactly as you intend them to operate later on in franchise units. The pilot operation should run for at least 6 months--sometimes for 12--in order to accumulate figures on sales, cost, and profit. You use these figures to evaluate the "typical unit" and determine the kind of franchise package you can offer.

HOW MUCH MONEY?

The statistics from your pilot outlet are the basis for determining how much money a franchise unit needs for four things: (1) cash flow, (2) building and equipment, (3) inventory, and (4) profit.

The amount of money which will be needed to insure proper cash flow in a franchise outlet hinges on the type of business. If sales build gradually--or if the franchisee has to extend credit to his customers--then he must have enough working cash to tide him over while his store builds a following. Of course, he will need less backup money if the cash return is immediate. Also bearing on his working cash will be the amount of inventory he needs to carry in order to serve customers efficiently.

Whether the franchisee needs money for a building and equipment depends on the individual circumstances of the franchise. If you pay for the building, for example and lease him equipment, then the burden of having a ready source of investment capital is on your shoulders.

Finally, you will need to use the figures from the pilot operation to determine profitability. How will the franchise program contribute to your company's profits? How much profit can the franchisee make on his store? It is vital to keep in mind that unless there is a profitable franchisee, there can be no franchisor.

THE FRANCHISE AGREEMENT

The findings from your operation of the pilot outlet will determine: (1) what the franchise fee will be, (2) the type of franchise agreement, and (3) the amount of working capital, over and above the franchise fee, that the franchisee will need to get his business started and on a paying basis. Franchise agreements are as varied as the franchise business itself, but agreements usually are of two general types.

One type is the operating franchise contract. With it, you allow the franchisee to operate one or several franchises but not to subfranchise. The second type is the area franchise arrangement. With it, you give the franchisee a large territory so he can engage in subfranchising.

Franchise contracts, regardless of their general type, vary to fit the situation. For example, if the franchise requires a relatively large investment in machinery which you manufacture, you may become a "partner" of the franchisee until the machinery is paid for from profits of the business. In other situations, franchisors may provide financial assistance to purchase the building which the franchise business needs to conduct its operation.

In writing a franchise agreement, you will want to work closely with your lawyer. Your contract should spell out the details, some of which are:

The franchise fee and other capital requirements.

The area of protection for the franchisee.

Financial assistance, if any, offered to the franchisee.

Your control over: (1) location of the business; (2) franchisee purchases; (3) performance; (4) quality and service standards; (5) physical appearance; (6) products carried other than the franchised line; (7) promotional activities; and (8) recommended prices.

Recordkeeping requirements.

Management assistance and training.

Sale of franchise license.

Termination of franchise.

UNDERSTANDING THE MARKET

In putting together and selling a franchise package, it is helpful to have a knowledge of your market--the kind of person who buys a franchise. As a rule, he has little or no knowledge of the field he is entering. He is uncertain about the future and wants to keep his risk as low as possible. He wants expert attention applied to his investment.

To fill these needs, he buys a franchise. From it he gets knowledge about a business with which he is usually unfamiliar and volume advantages--purchasing and advertising--offered by a successful company. Keeping the risk low is important to many franchisees. They are willing to accept lower returns on their investments in order to minimize the prospect of failure.

It is important to keep in mind that the buyer wants guidance. Furthermore, he is apt to feel that he has not gotten his money's worth if the franchisor does not, or cannot, supply the guidance which helps the outlet operate profitably.

The strength of your program depends on how well you help your franchisees. It is not enough for the franchisor to back off after he has helped, for example, to open the doors to a franchise restaurant.

SELLING THE PACKAGE

Three things are important in selling your franchise package--in getting investors who are qualified to work with your company. They are: the sales brochure, supplemental advertising, and screening prospects.

• The Sales Brochure

Your primary sales tool will be your franchise sales brochure. Your experience with the pilot franchise unit represents what you have to offer: your brochure tells the reasons why you are offering it. It will introduce prospects to your operation. Because many of them have little or no knowledge of your business the brochure should go into the details.

Your brochure can also serve as a public relations tool. It can supply information on your business to trade paper editors, newspapermen, real estate developers, suppliers, and others who need to know about your business. Thus your brochure should be attractive as well as factual and descriptive.

Professional assistance can be helpful in making it so. Keep in mind that a shoddy and cheap-looking brochure cannot sell a franchise which bears a price tag in the thousands of dollars. Professional help can also save you money on printing and mailing by advising on size and weight. In one year, a restaurant franchisor mailed more than 9,500 brochures to interested persons even though it had only 30 franchises to grant.

• Supplemental Advertising

In addition to printing a brochure, you will need to advertise the fact that franchises are available. You should select media which are seen by the type of person you want to interest. If you are seeking an unskilled person who can be taught to run a low-investment business, then a consistent schedule of ads in the classified section of the newspaper is probably a good approach.

However, if your franchise package has a relatively high cost and requires a specific ability, your advertising should be pinpointed. You will need display ads on financial pages or ads in specialized publications.

- Screening Prospects

When your advertising and brochure have generated a list of interested prospects, your next task is to pick the best prospects. You should screen these carefully because the franchisor-franchisee relationship is on a long-term basis, usually 10 years or more.

Each applicant has to be evaluated as to character, health, stability, willingness to work, and financial standing. He should be evaluated also on his ability to get along with people because he will be dealing with both the public and employees--and in your name.

Personal interviews are a good way to do the basic screening. Prospects who pass this screening should be interviewed again in a longer and more penetrating meeting. It is a good idea to include the prospect's wife because she plays an important role in the franchise business and should be aware of the problems that can arise in operating a franchise unit.

Your interviews should be give-and-take sessions. Be prepared to answer the prospect's questions about the financial status of your company, future development plans, product quality, price, the franchise territory, payments, type of assistance you will provide, advertising costs, and lease agreements.

Sometimes, the prospect may bring his lawyer to the early interviews. If he doesn't, you should insist that the franchisee have a lawyer to advise and represent him when the contract is signed. Such advice helps to prevent misunderstandings later on.

TRAINING THE FRANCHISEE

After the agreement has been signed, your new franchisee will be eager to get started, and he should be moved into his training while his interest is still high.

Training him in your way of doing business is important because you and your other franchisees suffer when one franchisee falls down on the job. Training should stress that the rewards are there for persons with ability, initiative, and endurance.

You will want to keep in mind that the indidividual franchisee's actions, in the long run, determine the success or failure of a franchise program. When he reflects the proper training in the management of his outlet, franchising can indeed be a lever for accelerating the growth of the franchisor.

FOR FURTHER INFORMATION

Businessmen interested in exploring further the subject of franchising may be interested in the following references. This list is brief and selective. However, no slight is intended toward authors whose works are not mentioned.

The Franchise Annual, 1965. $2. National Franchise Reports, 333 North Michigan Avenue, Chicago, Ill. 60601.

The Franchise System of Distribution. 1963. (A research report sponsored by the Small Business Administration). $2.50. Research Division, School of Business Administration, University of Minnesota, Minneapolis, Minn. 55455.

"The Franchise System of Distribution," *Management Research Summary* No. 172. Free. Small Business Administration, Washington, D.C. 20416 (or nearest SBA office).

The Franchise Boom: How You Can Profit In It. Harry Karsh. 1962. $7.95. Prentice-Hall, Inc., Englewood Cliffs, New Jersey 07631.

Modern Franchising Magazine. $3 per year. Modern Franchising Magazine, Inc., 1085 Walnut Street, Des Plaines, Ill. 60016.

Franchise Company Data. Task Force for Equal Opportunity in Business. October 1965. U.S. Department of Commerce, Washington, D.C. 20230.

Still another source of information is the International Franchise Association, Inc., 330 North Michigan Ave., Chicago, Ill. 60601.

Small Business Administration
COUNSELING NOTES

FRANCHISED BUSINESSES

A franchise contract is a legal agreement to conduct a given business in accordance with the franchisor's prescribed operating methods, financing systems, territorial domains, and commission fees.

Franchise systems are getting more and more popular as a method of doing business. Most of them are in retail and service fields. Many are in food lines such as restaurants, luncheonettes, ice-cream or frozen-custard stands, and pizza, hot-dog, hamburger, and soft-drink bars. Others are in the fields of slenderizing, laundering, drycleaning, various kinds of repairing, and tax accounting.

The automobile industry has produced franchises in seat covering, auto muffling, carwashing, car renting, and even car selling, though dealerships in car retailing are much more difficult to obtain than most franchises. Franchises can now be had in swimming-pool contracting, service clubs, tool renting, and many types of distribution arrangements. In fact, some aspects of this way of doing business are found in almost every field.

A franchise generally offers some real advantages as an approach to entering a business of your own. You are given the benefit of the franchisor's experience and help in choosing a location, financing, marketing, recordkeeping, and in promotional techniques. The business starts out with an established product or service reputation. It is organized and operated with the advantages of "name" and standardization.

But not even all this can guarantee success. You yourself will still be primarily responsible for the success or failure of your venture. You will need certain personal qualities--management ability, willingness to work long hours, determination in the face of setbacks, and particularly the knack of foresight for planning against changes in location, markets, tastes, and economic conditions.

Before signing a franchise contract, you need to know a good deal about the parent chain--about its products, services, markets, and claims. Remember that when you accept a franchise, you bind yourself legally to a set of conditions you may later regard as not being to your advantage. Be wary of advertisements describing too-high returns or exaggerated successes and of those giving little information about the franchise system. In any case, get the advice of a lawyer before you sign a formal agreement.

Here are some publications that should be helpful:

Facts About Franchising. Free. Include stamped return envelope. National Better Business Bureau, 230 Park Ave., New York, N. Y. 10017.

The Franchise Boom: How You Can Profit in It, by Harry Kursh. 1962. $7.95. Prentice-Hall, Inc., Englewood Cliffs, N. J. 07632.

Franchise Company Data. Prepared by the Task Force for Equal Opportunity in Business. October 1965. Free. U.S. Department of Commerce, Washington, D.C. 20230.

The Franchise System of Distribution, by E. H. Lewis and R. S. Hancock. A report of research sponsored by the Small Business Administration. 1963. $2.50. University of Minnesota, School of Business Administration, Minneapolis, Minn. 55455. A 4-page summary of the report is available free from the Small Business Administration, Washington, D.C. 20416, or from any SBA field office. Ask for MRS-172: The Franchise System of Distribution.

Modern Franchising Magazine. Published bimonthly. $2.00 a year. Modern Franchising Magazine, Inc., 1085 Walnut St., Des Plaines, Ill. 60016.

National Franchise Reports. Monthly. $12.00 a year. The Franchise Annual. $2.00. International Franchise Association, Inc., 333 North Michigan Ave., Chicago, Ill. 60601.

The following SBA publications may be obtained from the Small Business Administration, Washington, D.C. 20416, or from any SBA field office.

Are You Ready for Franchising? by A. L. Tunick. Small Marketers Aid No. 115. October 1965. Free.

SBA-115A: Free Publications and SBA-115B: For-Sale Booklets. Lists of publications issued by the Small Business Administration. Free.

CN 3: 2/66 rev.

GOING INTO BUSINESS:

The new look in franchising

SIX YEARS AGO, Marine Col. William C. Humberd's future looked pretty well set. Rounding out his 23rd year as a Marine pilot, he was commanding officer of the Air Station at New River, N.C., and well on his way to a 30-year service career. But a heart attack in 1962 changed all that. Suddenly he was faced with early retirement and the necessity of choosing a new career. The choice, franchised Mister Donut shops, finds him five years after retirement running a business of his own that will gross about a quarter of a million dollars this year and should reach more than $350,000 next year.

Bill Humberd represents the new breed that is taking over where "Mom and Pop" left off in the booming franchise industry. Today's investors tend to be younger, better educated, more aggressive and more solid financially than their counterparts of 10 or 15 years ago. Moreover, they are benefiting from a trend that is becoming apparent in all major franchise operations: People who are notably successful with a franchised business are being permitted, even encouraged, by the parent companies to expand and develop local chains-within-chains.

Not long ago, the companies tended to restrict a franchise to a single operation. If there was business enough in the area to support a second shop, they were likely to divide the territory and sell a second franchise to another operator. Now they are recognizing that the man who was successful with the first operation is the man most likely to make a go of the second. He is experienced, he has proved his management ability and willingness to work, and he has usually built up some capital to finance his expansion.

Moreover, the old system led to a talent drain. Top-quality men got restless when they bumped into a ceiling on business growth; often they sold out and started anew in some more promising venture. Removing the limits helps keep the star players on the team.

According to Rogers Sherwood, publisher of *National Franchise Reports,* franchisees in service fields, such as carpet cleaning, have developed volume running into hundreds of

October 1967 Reprinted by CHANGING TIMES The Kiplinger Magazine, 1729 H St., N. W., Washington, D. C. 20006
COPYRIGHT © 1967 THE KIPLINGER WASHINGTON EDITORS, INC.

thousands of dollars annually through the appointment of subdealers. He says that franchisors in many areas—McDonald's (hamburgers), Midas (auto parts replacement shops), AAMCO (transmission repair shops) and H & R Block (income tax preparation), for example—can point to franchisees who have developed million-dollar businesses.

A quick road to riches?

NET PROFITS in a well-established franchise may run from 15% to 20% of gross income, and an exceptionally successful franchisee may increase his profit margin to 30% or even 40%. But no ethical franchisor *guarantees* that you'll have any profit at all, though to protect his own reputation and keep his own profits coming, he'll do everything possible to see that you do.

The basic ingredients of success are still much the same as for Mom and Pop—long hours and hard work. To these, today's prosperous franchisee adds his own skills and experience, and the training, professionalism and sophisticated business techniques supplied by his franchisor. Like Mom and Pop, he starts with a small base, but if he's initially successful, he has the opportunity to grow.

Take a look at how it worked for Bill Humberd. About the only things certain when he retired from the Marine Corps were that he did not want to go into a defense industry and that he wanted to be his own boss. He moved to Weymouth, Mass., where he had once been stationed and which he and his wife had chosen for a retirement home. Then, he says, "I just began looking around, without anything definite in mind. I had never given it any real thought, because I expected to go for 30 years in the Marines."

A friend who had worked for the Mister Donut organization first suggested the franchise, and, "because franchising was beginning to become quite popular then," he got in touch with one of the company executives. After several meetings, he was sold on the idea and the company was sold on him. In January 1963, he reported to Mister Donut for an eight-week training program.

In March, he opened his first shop in Brockton, Mass., and for the first year spent most of his waking hours supervising its 24-hours-a-day, seven-days-a-week operation—a fairly typical situation for a franchisee. But he was not satisfied to stop there.

"There are many, many ways to sell doughnuts," he explains, "and I wanted to sell as many as possible. Volume is the whole thing, and I didn't care if they went out the front door or the back door, as long as I could fully utilize the shop's capacity and equipment."

Following that line of reasoning, he developed a wholesale business, supplying doughnuts to concessionaires in two discount stores and to snack bars in a small chain of stores. Then he opened a Mister Donut satellite, a shop that sells the product made in the Brockton store's kitchens. Last July, he was ready for further expansion, and bought a successful company-operated store in Braintree, Mass.

This most recent purchase firmly establishes Bill Humberd as a substantial businessman in his own right. His capital investment now totals more than $100,000, his payroll covers 55 full- and part-time employes, and he has acquired all the headaches, as well as the rewards, of a successful small businessman.

The biggest worry is getting and keeping competent help, and he has been fortunate in that respect. But managing and overseeing the operation is still his responsibility. To exercise it, he makes all deliveries himself. This gives him a chance to check on all the shops and outlets at least twice a day. And, though his hours are not as long as they were initially, he still works a six-day week. Even so, in 1966 he was able to take a five-week vacation (his first since he opened the business), and last spring he managed to work in a week's fishing in Maine.

The key to success, he feels, is learning from experience, both his own and that of the parent company, and using that knowledge to grow.

The role of the franchisor

IF THE CHAIN-WITHIN-A-CHAIN concept of franchising is profitable for the franchisee, it's equally so for the parent company. According to David B. Slater, president of Mister Donut and executive co-director of the Boston College Center for the Study of Franchise Distribution, franchisors are just beginning to realize what an asset a successful franchisee can be. "We want to expand," he says, "and we have 250 built-in substantial businessmen who want to grow. The potential is tremendous."

With each successful expansion, the risk of failure decreases for both franchisee and franchisor; and, for the franchisee especially, the opportunity for further growth increases. It's much easier to finance expansion from a $300,000 base than from a $40,000 one. Bill Humberd, for example, was able to offer $65,000 cash for his most recent franchise without resorting to parent-company financing. His ability to arrange his own financing signaled recognition of his standing as a businessman within his own community.

The fact that reputable franchisors have hundreds of "built-in, substantial businessmen" with whom they can expand is a mark of the coming of age of the franchise industry. Most franchisors will tell you candidly that in the early days just about anyone who had the money for a down payment could get into a franchised business. Now money is no longer the only criterion. The man is considered more important, and franchisors are developing sophisticated screening techniques designed not to get you into the business, but to keep you out if it seems that you can't make a go of it.

All prospective Mister Donut franchisees, for example, are given an extensive aptitude and interest test developed especially for the company by a national testing organization. By matching a candidate's test results with a profile of the 100 most successful franchisees, Mister Donut officials are able to judge fairly accurately whether he has a good chance of prospering. Other franchisors have developed similar programs. For these services they pay substantial sums in retainers and fees, but most feel they save money in the long run.

"Doughnuts are only the vehicle," explains Slater. "We're really in the *people* business and the better people we can attract, the better all of us will do. By screening them first, we can get people who are psychologically prepared for a franchise relationship. People who go into franchising have to give up some measure of independence. Those whom we get know the score, they understand the responsibility they have."

Before you sign up, read up

Until recent years, there was a dearth of information on the franchise industry. Now the situation is improving, and you can find out a lot about how a franchise operates before you get to the contract-signing stage.

The Boston College Center for the study of Franchise Distribution, established two years ago, conducts annual management conferences on franchising and has a collection of written material on franchising. Its bibliography for prospective franchisees or franchisors includes the following:

Franchising Today 1966-1967, report of the 1966 conference, edited by Charles L. Vaughn and David B. Slater; $18.50 from Matthew Bender & Co., 235 E. 45th St., New York, N.Y. 10017.

The Franchise Boom, How You Can Profit in It, by Harry Kursh; available in libraries or for $7.95 from Prentice-Hall, Inc., Englewood Cliffs, N.J. 07632.

Franchising Agreements, hearings before the Senate Judiciary Committee's Subcommittee on Antitrust and Monopoly; $1.50 from Superintendent of Documents, Washington, D.C. 20402.

The following publications also will be useful:

Partners for Profit, A Study of Franchising, published by the American Management Association; $4.50 to AMA members, $6.75 to nonmembers from American Management Association, Inc., 135 W. 50th St., New York, N.Y. 10020.

Are You Ready for Franchising? by A. L. Tunick, Small Marketers Aids No. 115, published by the Small Business Administration and available free from SBA offices.

Some Socio-Economic Footnotes on Franchising, by David B. Slater, free from Mister Donut, 89 Providence Highway, Westwood, Mass. 02090.

National Franchise Reports, a monthly newsletter with current information on the industry and a list of new offers; $12 a year, $7 for a six-month trial, from National Franchise Reports, 333 N. Michigan Ave., Chicago, Ill. 60601.

Modern Franchising, a bi-monthly magazine designed for both franchisors and franchisees; $3 annually from Modern Franchising, Inc., 1033 First Ave., Des Plaines, Ill. 60616.

In return for sacrificing a measure of independence, the franchisee receives the benefits of the strengths and techniques of a large corporation if he is dealing with a good company. For example, a Mister Donut franchisee can expect professional and technical advice on such diverse matters as finances and real estate, employe relations and insurance. He must take and graduate from the company's eight-week training course (he's paid $100 a week while there). If he fails to make the grade at the school, his money will be refunded and he will not be awarded the franchise.

Once his franchise is a going business, he can expect a continuing relationship with the company along the same lines. A series of loose-leaf company manuals will keep him up-to-date on every phase of his business and on company policy and procedures. A computerized accounting system will help him catch his soft spots. He'll be able to offer new products that result from the efforts of a full-time research and development staff. He'll be the beneficiary of a nationwide advertising program, and he'll be supplied regularly with materials for local advertising and promotion. Most important, he'll have a constant and direct line of communication with his franchisor, both through its territory representatives and with the company executives themselves.

In return for this, he is expected to give up what Mister Donut's president terms "the inalienable right to *mismanage* his own business." After his first year in business, he is not required to buy his raw materials from Mister Donut sources, but he does have to purchase ingredients of comparable quality. As a practical matter, most franchisees do buy from the company's approved suppliers, where they can be sure of getting the correct mix. The franchisee must meet Mister Donut requirements for cleanliness and for courteous, efficient service. In short, he is expected to run a shop that conforms to company policy, company image and a nationwide reputation.

The details of the selection and training process, of the services furnished by the parent company, and of the responsibilities of the franchisee differ from company to company. But the general pattern tends to be much the same among the established franchisors.

Is franchising for you?

THE GREATEST ADVANTAGE of franchising is that it enables you to go into business with a great deal less capital and experience than you would need if you were on your own. But there are many pitfalls, and more than one franchisee has lost his savings on an ill-advised venture.

The International Franchise Association, organized seven years ago, has adopted a strict code of ethics, which, ideally, the entire industry should adhere to. Yet, despite its best efforts and those of individual franchisors, unethical operators are still around. These outfits will take your money, perhaps deliver you some equipment or materials, and then abandon you to your fate.

Both the IFA in Chicago and the Boston College Center at Chestnut Hill, Mass., are directing their attention toward ridding the industry of the fast-buck artists, but until they succeed, you're best advised to move cautiously. An ethical franchisor, incidentally, will insist that you do.

Franchises are available for virtually every type of business and for initial investments that range from a few hundred dollars to more than $100,000. Whether you're considering putting $500 in a vending machine business or $25,000 in a roadside food stand, investigate first.

As a starter, don't even bother to answer an ad that promises tremendous profits; be wary of a company that expresses interest only in your financial capability; and turn thumbs down on one that would allow you to tie up assets other than cash.

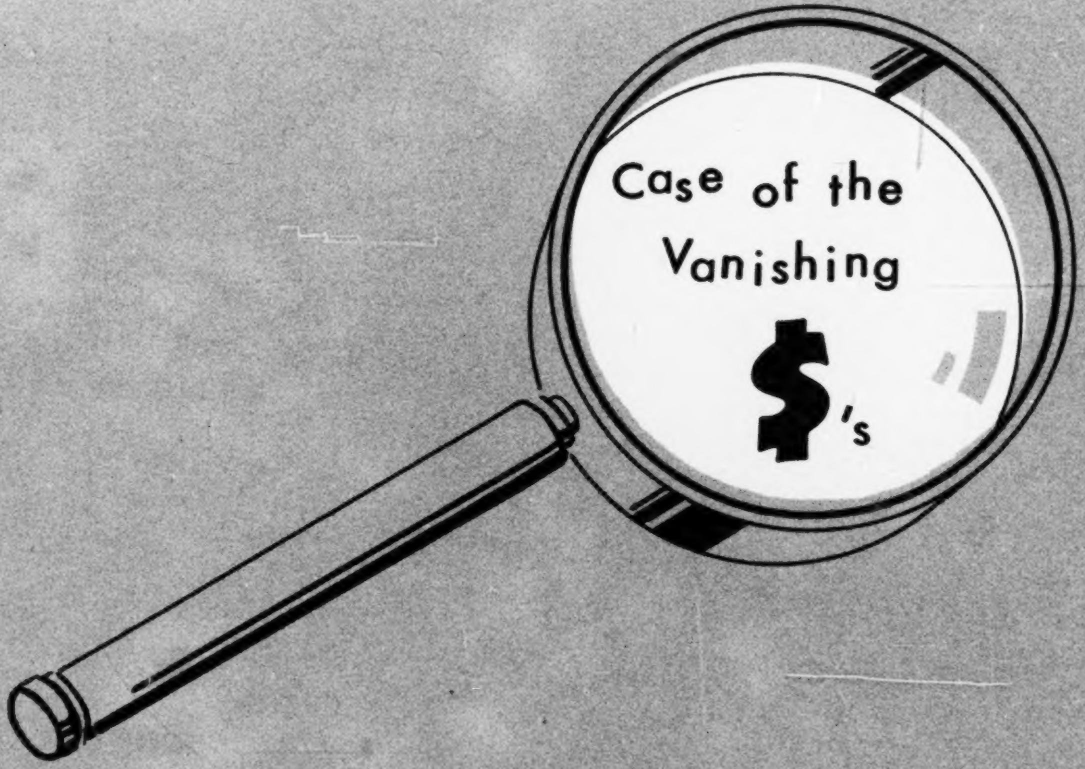
Investigate the franchisor—reputable ones welcome it. Find out what he offers in the way of initial guidance and training, and what system he has for the continuing relationship that's so important to success. The company will run a financial check on you; you're entitled to one on it. Ask for its bank references. Get its Dun & Bradstreet rating—if you can't get it yourself, your lawyer or banker can. Check with the Better Business Bureau on its standing.

Tour the home office. Find out what part research and development play in company operations, what accounting procedures are available to you. Get a list of franchisees, talk to them, ask what's wrong as well as what's right with their relationship to the franchisor.

Above all, get your lawyer to go over with you all the company literature as well as the contract. Be sure you understand the terms of renewal, termination and sale or transfer. Have terms of payments, royalties, purchasing and advertising spelled out in detail.

If the offering company balks at any of these steps, start looking elsewhere. Franchising may be the right business for you. You may be able to build your own chain-within-a-chain. But only if you land with a company that cares as much about your success as you do.

This article is reprinted by permission of Changing Times and may be reproduced locally for distribution to training participants.



CASES IN POINT

Case Studies for Depth Penetration

Section

The case method has proven stimulative and effective in many administrative management courses. The following case material is suggested as a means of encouraging discussion.

It is suggested that one full session be devoted to the presentation of the topic as outlined in this manual. A case can sometimes be used to stimulate or augment the discussion period that follows the presentation. This could be one way of expanding the basic materials into an advanced course on the subject.

THE CASE METHOD OF STUDY

The case method is a teaching device that helps the student learn through the processes of reasoning and decision making. Other popular teaching techniques stress learning or memorizing other people's knowledge on a given subject. The case method stresses thinking abilities rather than memory; it is dynamic, not passive.

What is a case? It is a description of an actual or true-to-life business situation. It is a statement of facts, opinions, judgments—in short, a problem having no pat answer but lending itself to discussion and analysis.

The case method is particularly helpful in teaching businessmen because it uses real, practical problems rather than abstract situations. Properly used, it involves the participants in a way that will hold their interest and stimulate their thinking. It is particularly useful in developing in the individual (1) the ability to make decisions on administrative tasks (without incurring the penalties of a wrong decision on the job); and (2) the habit of thinking analytically and constructively.

The case method also highlights the value of group discussion and analysis. Each member of the group contributes from his unique experience, and each participant gains from the others. The group's knowledge and experience will exceed that of any one participant—including the instructor.

The following checklist can serve as a procedure for conducting case study and analysis:

Suggestions for Case Study

1. Read the case carefully for general content.
2. Arrange the facts of the case in order of importance.
3. Recognize and define the major problem(s) needing solution.
4. Analyze the problems and their relative importance.
5. Search for and establish alternative solutions.
6. Select the most desirable of the appropriate solutions.
7. Analyze your probable solutions; set up the pros and cons, giving value to each.
8. State your choice, decision, or final conclusion—and be prepared to defend it.
9. Set forth the plan or plans you would follow to implement the decision.

CASE STUDY NO. 1

Fred Wilson was a labor union leader in a Midwest steel town, with 16 years of seniority on his job. He was well liked by his fellow workers, and found his dealings with management at the bargaining table interesting and challenging. But Fred did feel that he could go no farther in his job, and he and his wife talked often about a business of their own.

A newspaper advertisement of a drive-in restaurant franchise attracted Mrs. Wilson, and at her urging, Fred inquired about it. A meeting was arranged with a company representative, at which time the Wilsons were exposed to the company's management, sales territories, advertising policies, cost and profit projections, and financing arrangements. At the conclusion of the meeting, the Wilsons were convinced this was their golden opportunity.

The Wilsons did not have very much capital because Fred's salary had been invested in paying off the mortgage on their home as rapidly as possible, and they enjoyed the luxury of a fine automobile each year. However, the Wilson's credit was excellent, and they borrowed what they lacked from their local bank, setting up a rapid repayment schedule, just as they had done with their home. The projected income figures indicated to Fred that this was feasible.

Less than a month later, the former steel worker was listening to marketing experts, food technicians, and experienced accountants explain the franchise operation. The training period was brief, but quite thorough, and Fred decided that whatever he didn't quite understand at the moment he would learn as he went along. Filled with enthusiasm, Fred returned home, eager to enter into his new business.

In the initial few days of operation, a company representative helped him operate the business. Store traffic was excellent—Fred's enormous circle of friends began to patronize the establishment immediately, and the pleasure of being the "boss" masked the strain of the long hours in the new enterprise.

When the company's representative left, Fred and his wife both worked in the restaurant, and, although the traffic of the first few days slackened a bit, the Wilsons were still working a good 16-hour day. After the first 2 months, Fred and his wife felt that the strain on them was too great—Mrs. Wilson had not worked previously, and Fred was quite used to his comfortable 40-hour week. So the Wilsons made a decision to hire additional help to ease their burden.

Two new employees were hired and given a 2-day on-the-job training course by a franchisor company representative. By the end of the week, Fred was convinced that the new employees could handle the job, and he let them take over the evening shift.

After 2 weeks, it became apparent that this system wouldn't work—and the Wilsons split up the workday—Fred and one employee took one shift, and Mrs. Wilson and the other employee took the other shift. The system seemed practical—the customers were being served properly, and all looked well * * * until the Wilsons looked at their accounts.

The additional costs of the help, on top of the financial obligations the Wilsons faced to repay their initial investment, was not leaving them very much. They were working very hard, and realizing less money than Fred had earned at his previous job. The only decision the Wilsons could make was to let the help go, and continue to do all of the work themselves, on a 6-day week, 16 hours a day. By the time the sixth month had rolled by, Fred was searching earnestly for a buyer for his restaurant.

QUESTIONS

1. Based on the supplied information, what do you feel was the principal reason for the Wilson's disenchantment with their franchise?

2. How compatible was Fred Wilson's background with the type of business he entered?

3. What financial arrangements could have been made to ease the Wilson's financial burden? Explain.

4. What would you suggest as a solution to the problem facing the Wilsons?

COMMENTS ON QUESTIONS

1. In discussion, bring out the fact that the Wilsons were accustomed to a standard workweek, with a regular period of leisure time. The proper devotion to their own business demanded more of their time and energies than they were used to expending on the earning of a livelihood.

2. Elaborate on the difference between his well-established work habits in industrial employment with those required by his new business.

3. His repayment schedule could have been spread over a longer time base to lessen his immediate financial burden.

4. There is no concrete answer. Among the possibilities: The Wilsons could sell out, and Mr. Wilson could return to a job in industry.

   They could readjust their living pattern to one compatible with their new business, and try to obtain employees capable of reducing their workload.

   The answers to this question can provide worthwhile points for discussion in the classroom.

CASE STUDY NO. 2

Ron Schultz had been an insurance salesman, modestly providing for his wife and two sons. They resided in a modest Philadelphia neighborhood, and lived on the strict budget that many families find necessary with a limited income.

Schultz had been looking for a new field to enter—one that would permit him to expand his income basis. One of the opportunities he investigated was a franchise with one of the country's largest automatic transmission repair services, headquartered near his home.

Careful investigation revealed a growing market potential with very little competition. New car dealers were only equipped to handle the one make of transmission that they sold. And, because of their high overhead structure, transmission repair prices were quite high. Neighborhood garages that took in transmission repair work were farming it out to small shops that varied in quality, time, and cost. The potential was evident. But Ron was concerned with yet another problem—his lack of a mechanical background.

The franchisor's training program was designed to overcome just such preliminary doubts. An intensive 4-week program, the course consisted of 48 hours per week, covering employee recruiting, pricing, customer service, advertising, cost control and other vital details. The end result was to familiarize the franchisee with all aspects of the transmission service business, with an emphasis on *managing* transmission specialists, rather than teaching the actual mechanical work.

At the franchisor's suggestion, Ron selected several names at random from a list of the company's franchisees, and visited several of them at his convenience. Each of the franchisees seemed very pleased with his own business, and encouraged Ron to seek his own franchise with the company.

Further inquiry indicated that the location for the new franchise could be right in Ron's area. The tentative location was in a location that boasted 40,000 registered automobiles within a 30-minute ride of the shopsite. The initial cash investment that would be required for this franchise was $21,000, and the franchisor was ready to aid Ron in securing the financing. This investment would provide initial rental, substantial parts inventory, specialized tools, outdoor signs, utility deposits, office supplies, workbench, and shelving.

Continuing assistance offered by the franchisor included monthly conferences for all area franchise operators to review various phases of operations, weekly parts deliveries from the franchisor's warehouse, and a weekly review of sales progress and business proficiency.

The essential requirements Ron had to meet—besides his initial cash investment—were a strong desire to earn money and an ability to communicate with people.

QUESTIONS

1. List the advantages you can see in the franchisor's offer.
2. List the principal disadvantages you can see in the franchisor's offer.
3. What additional information can Ron obtain to aid him in making his decision?
4. What course of action would you recommend for Ron Schultz, based on the above information? Explain.

COMMENTS ON QUESTIONS

1. Among the advantages of the offer are:

   Growing market.
   Little competition.
   Comprehensive training program.
   Good location.
   Financial assistance.
   Continuing franchisor assistance.

2. Disadvantages of the offer are:

   Size of initial investment.
   Close supervision by franchisor.

3. Discussion-stimulating question. Possible sources for additional information include:

   Chamber of Commerce.
   National Franchise Reports.
   Franchise Consultants.
   Bank contacts.

4. General consensus should be that Ron Schultz should pursue the franchise opportunity.

THE INCUBATOR

A How To Do It

Section

Experience has shown that people achieve maximum benefit from a conference, staff meeting or training session when a period of incubation follows the implementation of the new idea, new information, or "new slant."

This is a do-it-yourself section that will allow the participants to try out or apply the ideas and information gained from this session.

This material may be reproduced locally for distribution to course participants.

INCUBATOR ASSIGNMENT

1. Visit your Chamber of Commerce or local Business Associations, and determine the following:
    - a. What has been the population growth in your community over the last 10 years?
    - b. What has been the pattern of business growth over the same time period?
    - c. What type of business enterprise has shown the best rate of growth?
    - d. What is the projected population growth in your community for the next 10 years?
    - e. What is the expected business growth in your community for the next 10 years?
2. List five different franchise businesses that impress you as having good potential in your community. List them in order of preference.
3. What are three important considerations in choosing a site to locate one of the above listed franchises?
4. What are several advantages—both business and personal—that you believe you would enjoy as a franchisee of one of the businesses you have listed?
5. What are the principal disadvantages you can foresee as a franchisee?
6. How many sources of investment capital can you find in your community? List them in order of potential.

BIBLIOGRAPHY

Topic—FRANCHISING

This is a selected list of references to books and periodicals that would be useful in locating and evaluating franchise opportunities. The list is necessarily brief and no slight is intended toward authors and other sources which are not included. An asterisk indicates material that was of substantial value in preparing this volume.

1. Curry, J. A. H., et al. *Partners for Profit, A Study of Franchising.* 1966. 128 pp. American Management Association, Inc., New York, N.Y. 10020 ($6.75).

2. *Directory of Franchising Organizations.* 1968. 64 pp. Pilot Industries, Inc., New York, N.Y. 10001 ($2).

3.* Finn, Richard P. "Franchising's Future". July/August 1966. *Income Opportunities Magazine,* Science and Mechanics Publishing Co., New York, N.Y. 10022.

4. *Franchise Company Data for Equal Opportunity in Business.* 1968. 124 pp. U.S. Department of Commerce. Superintendent of Documents, Washington, D.C. 20402. Free.

5. *Franchising Agreements,* Senate Antitrust and Monopoly Subcommittee, hearings. Superintendent of Documents, Washington, D.C. 20402 ($1.50).

6. Gross, Harry, and Levy, Robert S. *Franchise Investigation and Contract Negotiation.* 1967. 48 pp. Pilot Industries, Inc., New York, N.Y. 10001, ($2).

79

7.* Krush, Harry. *The Franchise Boom—How You Can Profit By It.* 1962. 273 pp. Prentice-Hall, Inc., Englewood Cliffs, N.J. 07632 ($7.95).

8. Laughlin, Charles W. "Legal Services for Small Retail and Service Firms". 1965. 4 pp. *Small Marketers Aids No. 118.* Small Business Administration, Washington, D.C. 20416. Free.

9.* Lewis, Edwin H. and Hancock, Robert S. *The Franchise System of Distribution.* 1963. 95 pp. Small Business Administration Management Research Report. School of Business Administration, University of Minnesota, Minneapolis, Minn. 55455 ($2.50).

10. *Modern Franchising.* Published bimonthly. Modern Franchising Magazine, Inc., Des Plaines, Ill. 60016 (six issues $3; single copy 50 cents).

11. Munsinger, Gary M. "Franchising: An Alternative to Independent Operation". November 1967. pp. 10–14. *Arizona Review,* University of Arizona, Tucson, Ariz. 85721. Free.

12. *National Franchise Reports.* Published monthly. National Franchise Reports, Chicago, Ill. 60601 ($12 a year).

13.* Scherer, D. J. *Financial Security and Independence Through a Small Business Franchise.* Rev. ed. 1967. 48 pp. Pilot Industries, Inc., New York, N.Y. 10001 ($2).

14. Shaw, Dale. "Big Money Is Waiting to Help You Go Boom—or Bust—With a Franchise". November 1966. True Magazine, Fawcett Publications, Greenwich, Conn. 06830.

15. Small, Anne, and Levy, Robert S. *A Woman's Guide to Her Own Franchised Business.* 1967. 47 pp. Pilot Industries, Inc., New York, N.Y. 10001 ($2).

16. Small, Samuel. "Starting a Business After 50". 1967. 40 pp. (Shows how to establish a franchised business and lists over 175 franchise opportunities). Pilot Industries, Inc., New York, N.Y. 10001 ($2).

17.* "The Franchise Business". 1965. 8 pp. *Small Business Reporter.* Bank of America, Small Business Advisory Service, San Francisco, Calif. 94120. Free.

U.S. GOVERNMENT PRINTING OFFICE : 1968—O-315-780

SMALL BUSINESS ADMINISTRATION FIELD OFFICES

Agaña, Guam
Albuquerque, N. Mex.
Anchorage, Alaska
Atlanta, Ga.
Augusta, Maine
Baltimore, Md.
Birmingham, Ala.
Boise, Idaho
Boston, Mass.
Buffalo, N.Y.
Casper, Wyo.
Charleston, W. Va.
Charlotte, N.C.
Chicago, Ill.
Cincinnati, Ohio
Clarksburg, W. Va.
Cleveland, Ohio
Columbia, S.C.
Columbus, Ohio
Concord, N.H.
Dallas, Tex.
Denver, Colo.
Des Moines, Iowa
Detroit, Mich.
Dover, Del.
Fargo, N. Dak.
Hartford, Conn.
Hato Rey, Puerto Rico
Helena, Mont.
Honolulu, Hawaii
Houston, Tex.
Indianapolis, Ind.
Jackson, Miss.
Jacksonville, Fla.
Kansas City, Mo.
Knoxville, Tenn.
Las Vegas, Nev.
Little Rock, Ark.
Los Angeles, Calif.
Louisville, Ky.
Lubbock, Tex.
Madison, Wis.
Marquette, Mich.
Marshall, Tex.
Miami, Fla.
Milwaukee, Wis.
Minneapolis, Minn.
Montpelier, Vt.
Nashville, Tenn.
Newark, N.J.
New Orleans, La.
New York, N.Y.
Oklahoma City, Okla.
Omaha, Nebr.
Philadelphia, Pa.
Phoenix, Ariz.
Pittsburgh, Pa.
Portland, Oreg.
Providence, R.I.
Richmond, Va.
St. Louis, Mo.
Salt Lake City, Utah
San Antonio, Tex.
San Diego, Calif.
San Francisco, Calif.
Seattle, Wash.
Sioux Falls, S. Dak.
Spokane, Wash.
Syracuse, N.Y.
Toledo, Ohio
Washington, D.C.
Wichita, Kans.

NOTE: The addresses and telephone numbers of these field offices are listed under U.S. Government in the respective city telephone directories.

◆ GRAY — The Lesson Plan

◆ RUST — The Presentation

◆ BUFF — The Visual Aids

◆ GREEN — The Supply Department

◆ YELLOW — Cases in Point

◆ BLUE — The Incubator

ERIC Clearinghouse
MAR 21 1972
on Adult Edu